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IN THE

# Supreme Court of the United States

THOMAS R. PHILLIPS, Chief Justice, NATHAN R. HECHT, Justice, CRAIG T. ENOCH, Justice, PRISCILLA R. OWENS, Justice, JAMES A. BAKER, Justice, Justice, DEBORAH G. HANKINSON, Justice, HARRIET O'NEILL, Justice, and XAVIER RODRIGUEZ, Justice, in their official capacities as Justices of the Supreme Court of Texas, TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; and RICHARD TATE, in his official capacity as Chairman of the Texas Equal Access to Justice Foundation,

*Petitioners,*

v.

WASHINGTON LEGAL FOUNDATION, WILLIAM R. SUMMERS, AND MICHAEL J. MAZZONE,

*Respondents.*

**ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT**

## PETITION FOR A WRIT OF CERTIORARI

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## QUESTIONS PRESENTED

1. Whether the Texas Interest on Lawyers' Trust Accounts ("IOLTA") program "takes" private property within the meaning of the Just Compensation Clause of the Fifth Amendment.

2. Whether a claimant who has suffered no economic loss is nonetheless entitled to relief, including injunctive or declaratory relief, under the Just Compensation Clause.

3. Whether the claims against the Chief Justice and Justices of the Supreme Court of Texas are subject to dismissal on grounds of official immunity.

## PARTIES TO THE PROCEEDING

The following were parties to the proceeding in the court of appeals: Chief Justice Thomas R. Phillips, Justice Nathan R. Hecht, Justice Craig T. Enoch, Justice Priscilla R. Owens, Justice James A. Baker, Justice Deborah G. Hankinson, Justice Harriet O'Neill, Justice Xavier Rodriguez, Texas Equal Access To Justice Foundation, Chairman Richard Tate, Washington Legal Foundation, William R. Summers, and Michael J. Mazzone.

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## PETITION FOR A WRIT OF CERTIORARI

The Chief Justice and Justices of the Texas Supreme Court, the Texas Equal Access to Justice Foundation ("TEAJF"), and Richard Tate, in his official capacity as the Chairman of TEAJF, respectfully petition this Court for a writ of certiorari to review the decision of the United States Court of Appeals for the Fifth Circuit in this case.

## OPINIONS BELOW

The opinion of the court of appeals is reported at 270 F.3d 180 (5th Cir. 2001). Appendix ("App."), *infra*, 1a-43a. The opinions dissenting from the denial of rehearing en banc are not yet reported but are reprinted in the Appendix, *infra*, at 169a-194a. The opinions of the district court are reported at 86 F. Supp. 2d 617 and 86 F. Supp. 2d 624 (W.D. Tex. 2000). App., *infra*, 86a-99a, 44a-85a.

A prior opinion of this Court in this case, *Phillips v. Washington Legal Foundation*, is reported at 524 U.S. 156 (1998). App., *infra*, 100a-126a. A prior opinion of the court of appeals is reported at 94 F.3d 996 (5th Cir. 1996). App., *infra*, 127a-146a. An opinion dissenting from the denial of rehearing en banc is reported at 106 F.3d 640. App., *infra*, 195a-207a. The district court's initial opinion is reported at 873 F. Supp. 1 (W.D. Tex. 1995). App., *infra*, 147a-168a.

## JURISDICTION

The judgment of the court of appeals was entered on October 15, 2001. App., *infra*, 1a. A timely petition for rehearing was denied on May 31, 2002. App., *infra*, 169a. The jurisdiction of this Court is invoked pursuant to 28 U.S.C. § 1254(1).

## CONSTITUTIONAL PROVISIONS INVOLVED

The Fourteenth Amendment to the United States Constitution provides in relevant part:

> [N]or shall any State deprive any person of life, liberty, or property, without Due Process of law . . .

The Fifth Amendment provides in relevant part:

> [N]or shall private property be taken for public use without just compensation.

## STATEMENT OF THE CASE

This case is one of two cases currently before this Court concerning the constitutionality of Interest on Lawyers' Trust Accounts ("IOLTA") programs. In this case, the Fifth Circuit held that the Texas IOLTA program violates the Just Compensation Clause of the Fifth Amendment. The Court recently granted certiorari to review the other case, *Washington Legal Foundation v. Legal Foundation of Washington*, 271 F.3d 835 (9th Cir. 2001) (en banc), *cert. granted*, 70 U.S.L.W. 3580 (U.S. June 10, 2002) (No. 01-1325) ("*WLF v. LFW*"). In *WLF v. LFW*, the Ninth Circuit held that the State of Washington's IOLTA program does not violate the Just Compensation Clause. The Court should grant the petition in this case and consolidate it with *WLF v. LFW* for oral argument, so that the Court can consider the constitutional issues in the context of a fully-developed trial record.

As the Court knows from its prior consideration of this case, IOLTA programs have been adopted by all 50 States, the District of Columbia, and the Virgin Islands, and are a principal source of funding for civil legal services to low-income families and individuals. *See* App., *infra*, 100a-01a. In *Phillips*, the Court held that interest earned on IOLTA accounts is property of the client for purposes of the

Just Compensation Clause, but remanded for consideration of whether the property is "taken" in the constitutional sense by the IOLTA program, and if so what compensation, if any, is due under the Fifth Amendment. *Id.* at 113a-14a. The Court "express[ed] no view" on either question. *Id.*

On remand, the district court conducted a trial on the merits and held that there was no violation of the Just Compensation Clause, on the basis of its finding that plaintiffs could not prove a compensable financial loss under any accounting or economic theory. Holding that finding to be "not relevant," and a "non-factor in the taking analysis," *id.* at 13a n.6, a divided panel of the Fifth Circuit reversed. An evenly-divided en banc court denied the petition for rehearing by a vote of 7-7.

The seven dissenting Fifth Circuit judges expressed the hope that this Court would "address this very important case once again [to] resolve the questions left unanswered by its prior opinion." They concluded that review of the panel opinion is imperative in the light of (1) the disagreement between the Circuits; (2) the panel majority's "novel" approach to takings analysis, which has "far-reaching" implications; (3) the trial court's finding that plaintiffs have not shown "any compensable loss whatsoever," and (4) the effect on IOLTA programs that will likely result. *Id.* at 171a.

**The Facts Giving Rise To This Case**

Although IOLTA programs vary from State to State, they generally operate by aggregating client funds held in trust by lawyers in circumstances in which the funds cannot be made to earn interest for the clients, and then distributing the interest generated by the aggregated funds to non-profit organizations, most of which have the primary purpose of providing civil legal services to the poor.

The Texas Supreme Court established Texas's IOLTA program, known as the Texas Equal Access to Justice Program, in 1984. Client funds may not be placed in an IOLTA account unless there is no reasonable expectation that the funds can be made to earn interest for the client. *See* Texas Rules of the Court — State, Rules Governing the Operation of the Texas Equal Access to Justice Program Rule ("TEAJF Rule") 6 (West 1996). "By pooling client deposits that individually were so small or held for such a short period of time that they would not earn a net positive interest," IOLTA permits Texas and other States to "use the interest earned on the combined deposits — otherwise enjoyed as a windfall by the banks — to fund indigent legal services at no cost to the owner of the principal." *WLF v. LFW*, 271 F.3d at 843.

Under the Texas program, attorneys must review periodically whether changed circumstances require that their client's funds be removed from the IOLTA account. TEAJF Rule 6. If the attorney determines that the funds were erroneously placed into an IOLTA account, the attorney must notify TEAJF and obtain a refund of the interest earned. App., *infra*, 6a.

**A. Initial Proceedings.**

A single client, his lawyer, and a public interest group filed this action challenging the constitutionality of Texas's IOLTA program. The district court, which had subject-matter jurisdiction pursuant to 28 U.S.C. § 1331, entered summary judgment for the defendants. App., *infra*, 44a. On appeal, the Fifth Circuit vacated in part and remanded, holding that interest earned on funds held in IOLTA accounts is property of the client for purposes of the Just Compensation Clause. App., *infra*, 1a.

**B. This Court's Decision In *Phillips*.**

This Court granted review and affirmed. *Phillips v. Washington Legal Foundation*, 524 U.S. 156 (1998) (App., *infra*, 100a). Observing that principal deposited in IOLTA accounts belongs to the clients, and invoking "[t]he rule that 'interest follows principal,'" this Court held that interest earned on IOLTA accounts is property of the client for purposes of the Just Compensation Clause. *Id.* at 106a. The Court remanded for consideration of two additional questions, stating explicitly: "We express no view as to whether these funds have been 'taken' by the State; nor do we express an opinion as to the amount of 'just compensation,' if any, due respondents." *Id.* at 113a-14a.

In a dissenting opinion for four members of the Court, Justice Souter viewed both the "taking" and the "just compensation" questions as "serious ones for [plaintiffs.]" *Id.* at 118a. As to the "taking" question, Justice Souter observed that "we start with *Penn Central Transp. Co. v. New York City*, 438 U.S. 104 (1978)." *Id.* "[A]pplication of *Penn Central* would not bode well" for the plaintiffs, because this case involves "no physical occupation or seizure of tangible property," "no apparent economic impact," and nothing even "resembling an investment" or a "basis for reasonably expecting to obtain net interest." *Id.* at 118-19a.

As to just compensation, the dissent noted that "the client's inability to earn net interest outside IOLTA . . . raises serious questions about entitlement to any compensation." *Id.* at 119a. "[A] court presumably would look to the claimant's putative property interest as it was or would have been enjoyed in the absence of IOLTA," and "would measure any required compensation by the claimant's loss, not by the government's (or the public's) gain." *Id.* at 119a-20a (citing, *inter alia*, *United States v. 564.54 Acres of Monroe & Pike County Land*, 441 U.S. 506, 510 (1979); *Kimball Laundry*

*Co. v. United States*, 338 U.S. 1, 5 (1949); *Boston Chamber of Commerce v. City of Boston*, 217 U.S. 189, 194-95 (1910)).

**C. The Trial.**

On remand, the district court held a trial on the merits, made findings of fact, and answered both questions left open by this Court in favor of the defendants. App., *infra*, 44a. The district court considered and rejected plaintiffs' evidence that Respondent Summers (the client plaintiff) could have earned interest based on "in-firm pooling," "sub-accounting," or a "net benefit theory." The district court found that Respondents "failed to present any evidence that Mr. Summers' money . . . did and could generate net benefit, or net interest if not for IOLTA. Plaintiffs failed to establish an actual number denominating Mr. Summers' loss. With regard to *this case* and *Mr. Summers'* monies, Plaintiffs have failed to carry their burden of proof." *Id.* at 77a. (emphasis in original). "[B]ased upon all the evidence before it," including Mr. Summers's own admission that "he was no worse off because of IOLTA," the Court found as a fact that "Mr. Summers's loss is zero." *Id.* at 67a, 77a. The court held that just compensation for a loss of zero is zero.

The district court also held that no "taking" had occurred. It held that per se taking analysis is not appropriate, distinguishing this case from cases such as *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982), that involved "the physical invasion of real property," and finding *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155 (1980), to be "easily distinguishable"

because here "there is no money to confiscate outside the mechanisms which make IOLTA possible." *Id.* at 82a.[1]

The district court also granted the motion of the Chief Justice and Justices of the Supreme Court of Texas for judgment on the pleadings based on their official immunity. Relying on *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719 (1980), the district court found that the members of the Supreme Court of Texas were acting in a legislative capacity because they have no independent power to enforce the TEAJF program rules. On the basis of this fact, the district court held the Justices to be absolutely immune from this suit. App., *infra*, 86a.

**D. The Fifth Circuit's Decision.**

A divided panel of the Fifth Circuit reversed. The panel majority viewed this Court's decision in *Phillips* as dispositive, and therefore viewed the district court's findings of fact as irrelevant. *See* App., *infra*, at 14a ("[T]he linchpin for this case has already been inserted by the Supreme Court"); *id.* at 13a n.6 (findings of fact on economic loss "not relevant" "in the light of *Phillips* and *Loretto*"). As to the taking question, the panel majority held that application of per se taking analysis is compelled by *Phillips* and two decisions it cites, *Webb's* and *Loretto*. The court distinguished a line of this Court's decisions holding that per se analysis does not apply to a "governmental appropriation of money" on the ground that those cases involved fees for government services. *See id.* at 12a.

As to just compensation, the panel majority held that "once a taking is found, the question becomes what amount

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[1] The district court rejected Respondents' additional claim that the TEAJF program violates the First Amendment. App., *infra*, 55a-64a. The Fifth Circuit did not reach this issue.

of, not whether, just compensation is due." *Id.* at 15a (citing *Phillips* and *Loretto*). The court of appeals did not question the trial court's factual finding that the plaintiffs suffered no economic loss (*id.* at 12a-13a), nor did it attempt to quantify the amount of just compensation due to Mr. Summers. Instead, the court noted that Petitioners are entitled to Eleventh Amendment immunity, and therefore Respondents "seek only prospective declaratory and injunctive relief." *Id.* at 17a.

The court of appeals proceeded to consider whether equitable relief is appropriate in this case, and held that it is because Petitioners had conceded, at an earlier stage of the litigation, that they were "subject to [plaintiffs'] prospective injunction claims." *Id.* at 17a. In addition, the court held that Respondents are not required to seek just compensation from the State of Texas, although it recognized that the contrary view "has some support." *Id.* at 18a. The court of appeals also held that the Chief Justice and Justices of the Supreme Court of Texas are not protected by legislative immunity. *Id.* at 26a-27a.

Judge Wiener dissented. As an initial matter, he disagreed that Petitioners had conceded plaintiffs' entitlement to equitable relief. *See id.* at 29a ("The [Petitioners] have done no such thing.") Judge Wiener observed that there is "a vast difference between conceding that the Eleventh Amendment is not a *bar* to the assertion of a *claim*, on the one hand, and conceding *entitlement* to the *relief sought* by asserting a claim, on the other." *Id.* (emphasis in original). Judge Wiener commented that the trial has "brought us to precisely the moment Justice Souter foretold by proving that [the plaintiffs'] loss–and, therefore, the "just compensation that they are due–is zero." *Id.* at 28a. Applying the "constitutional truism" that "[t]he Fifth Amendment does not proscribe the taking of property; it proscribes taking without just compensation," Judge Wiener

concluded that the Texas IOLTA program does "not violate the plaintiffs' constitutional rights because just compensation for zero is zero." *Id.* (internal quotation and citation omitted); *id.* at 36a ("when the owner's loss is zero, he is owed no compensation.").

### E. The Denial of the Petition for Rehearing.

Petitioners filed a petition for rehearing en banc on October 27, 2001. On May 31, 2002, an evenly-divided Fifth Circuit denied the petition by a 7-7 vote, with Chief Judge King and Judges Jolly, Wiener, Benavides, Stewart, Parker, and Dennis dissenting from the denial of rehearing en banc. Judge Higginbotham recused himself from the case.

The seven dissenting judges noted the "split in the circuits, [the] 2-1 reversal of the district court, and the far-reaching, exceptionally important constitutional and practical consequences of the Fifth Amendment jurisprudence thus established for this circuit by but two of our judges." The seven judges expressed the hope that "the Supreme Court will see fit to address this very important case once again and resolve the questions left unanswered by its prior opinion." App., *infra*, 171a.

Judge Wiener, joined by five additional judges, supplemented his prior dissent from the panel opinion. Judge Wiener's opinion faulted the majority's legal analysis as being completely divorced from the district court's factual finding "that plaintiffs could not prove any amount of monetary loss under any accounting or economic theory." App., *infra*, 174a.

### F. The Ninth Circuit's *En Banc* Decision in *WLF v. LFW.*

After the Fifth Circuit panel issued its decision in this case, and before it denied the petition for rehearing en banc,

the Ninth Circuit, sitting *en banc*, issued a decision in parallel litigation challenging the State of Washington's IOLTA program. *WLF v. LFW*, 271 F.3d 835 (9th Cir. 2001). Unlike the Fifth Circuit, which viewed this Court's decision in *Phillips* as effectively deciding the "taking" and "just compensation" questions, the Ninth Circuit recognized that this Court explicitly declined to express any view on those questions. *Id.* at 845, 853 (citing *Phillips*, 524 U.S. at 172).

On the "taking" question, the Ninth Circuit held that per se taking analysis does not apply in the IOLTA context. The per se approach, the court observed, "has not typically been employed outside the context of real property" and "is a particularly inapt analysis when the property in question is money." 271 F.3d at 854. Citing *United States v. Sperry Corp.*, 493 U.S. 52 (1989), and *Eastern Enterprises v. Apfel*, 524 U.S. 498 (1998), as well as the decisions of other courts of appeals, the court concluded that money, because of its fungibility, "differs from physical property in respects significant to takings analysis." 271 F.3d at 854. The Ninth Circuit concluded that this Court in *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155 (1980), "used the *ad hoc* analysis of *Penn Central* . . . as opposed to *Loretto*'s *per se* approach." 271 F.3d at 855.

Acknowledging that the Fifth Circuit panel had reached a different conclusion, *id.* at 856-57, the Ninth Circuit held that application of the *Penn Central* analysis was not only "appropriate" but "compelled." *Id.* at 857. The Ninth Circuit concluded that IOLTA programs present "the very circumstances for which the *Penn Central* analysis was intended." *Id.* IOLTA programs adjust "the benefits and burdens of economic life to promote the common good." *Id.* (quoting *Penn Central*, 438 U.S. at 124). Moreover, the highly regulated nature of the banking industry makes it less

likely that owners of principal would expect their property to remain wholly undisturbed. 271 F.3d at 856.

Applying the *Penn Central* factors, the Ninth Circuit held first that the IOLTA program had no economic impact on the plaintiffs because the funds deposited in IOLTA accounts were incapable of earning net interest for the principal-holders. *Id.* at 857-58. "Indeed," the court concluded, "if there be any economic impact, it is a positive one," because the program requires participants to place client funds in interest-bearing accounts if they are capable of earning net interest. *Id.* at 857. Second, the court held that the IOLTA program did not interfere with the plaintiffs' investment-backed expectations, because the plaintiffs could not have expected their principal to earn net interest outside of IOLTA. *Id.* at 860. Third, the Ninth Circuit held that the IOLTA program should not be characterized as a physical invasion of property, but instead as a regulation of the uses of certain property in the context of two commercial fields (banking and the practice of law) that are already pervasively regulated. *Id.* at 860-61. The court observed that the plaintiffs were not "being singled out to bear a burden that should be borne by the public as a whole," particularly given that none of the plaintiffs suffered *any* economic loss. *Id.* at 861. The court therefore held that Washington's IOLTA program did not "take" plaintiffs' property.

The Ninth Circuit went on to provide a second basis for its judgment. "Even if [the plaintiffs'] property was taken," the court noted, "the Fifth Amendment only protects against a taking without just compensation." *Id.* The court relied on Supreme Court decisions holding that just compensation must put "the owner of the condemned property in as good a position pecuniarily as if the property had not been taken." *Id.* at 862 (quoting *United States v. 564.54 Acres of Land*, 441 U.S. 506, 510 (1979), quoting, in turn, *Olson v. United States*, 292 U.S. 246, 255 (1934)).

Here, at most, IOLTA took away the plaintiffs' "opportunity to place the principal in a noninterest-bearing checking account." 271 F.3d at 863. But that loss is of no economic value, and is "'not compensable under the Fifth Amendment.'" *Id.* at 864 (quoting *United States ex rel. Tenn. Valley Auth. v. Powelson*, 319 U.S. 266, 281 (1943)). Therefore, the court held, "even if the IOLTA program constituted a taking of [the plaintiffs'] private property, there would be no Fifth Amendment violation because the value of their just compensation is nil." *Id.*[2]

On June 10, 2002, this Court granted the petition for certiorari in *WLF v. LFW*. *See* 70 U.S.L.W. 3580.

## REASONS FOR GRANTING THE WRIT

The decision below and the decision of the Ninth Circuit sitting en banc in *WLF v. LFW* are squarely in conflict on important questions of constitutional law that have immediate consequences for IOLTA programs and the legal services they fund, as well as far-reaching implications for all manner of government regulation. This Court has already granted review in *WLF v. LFW*, a case in which there is no trial record and no findings of fact. For that reason and others discussed in Part IV of this Petition, the Court should grant the petition in this case and consolidate it with *WLF v. LFW* for oral argument, so that the Court can consider the constitutional issues in the context of a fully-developed trial record.

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[2] The Ninth Circuit remanded for consideration of the Plaintiffs' First Amendment challenge. 271 F.3d at 864.

## I. THE FIFTH CIRCUIT'S HOLDING THAT IOLTA EFFECTS A PER SE TAKING CONFLICTS WITH THE NINTH CIRCUIT'S EN BANC DECISION AND THIS COURT'S PRECEDENTS.

In *Phillips*, this Court held that the interest earned on IOLTA accounts is property of the client but "express[ed] no view as to whether these funds have been 'taken' by the State." App., *infra*, 113a. Four Justices joined an opinion concluding that analysis of the "taking" question would "start with *Penn Central*." *Id.* at 118a (Souter, J., dissenting). Justice Souter's opinion observed that "application of *Penn Central* would not bode well" for Respondents, because IOLTA programs involve "no physical occupation or seizure of tangible property," "no apparent economic impact," and nothing even "resembling an investment" or a "basis for reasonably expecting to obtain net interest." *Id.* at 118a-19a. The Ninth Circuit's decision in *WLF v. LFW* follows the approach outlined in Justice Souter's opinion and holds that the Washington IOLTA program does not "take" private property.

The Fifth Circuit has taken a conflicting approach. It concluded that "*Phillips*, and *Webb's Fabulous Pharmacies, Inc. v. Beckwith*, 449 U.S. 155 (1980), and *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982), . . . compel applying the per se analysis." App., *infra*, 9a-10a. The Fifth Circuit did not dispute the district court's finding that Mr. Summers suffered "zero" economic loss, but held that this finding is simply "not relevant." *Id.* at 13a n.6. According to the Fifth Circuit, "the economic impact on the owner is a non-factor in the taking analysis." *Id.*

The Fifth Circuit erred in concluding that application of per se analysis is "compelled" by this Court's decision in *Phillips*. In *Phillips*, this Court expressly declined to state

any views on the question. Nor is application of "per se" analysis compelled by *Loretto* or *Webb's*. *Loretto* concerned a physical invasion of real property; this case involves neither real property nor a physical invasion. (Indeed, a "physical invasion" of intangible property is a contradiction in terms.) And *Webb's* (which was decided before *Loretto*) cites and relies on the *Penn Central* factors. 449 U.S. 155.

The Ninth Circuit disagreed that per se analysis applies in the IOLTA context. The per se approach, the court observed, "has not typically been employed outside the context of real property," and "is a particularly inapt analysis when the property in question is money." 271 F.3d at 854. Unlike the Fifth Circuit, the Ninth Circuit concluded that this Court in *Webb's* "used the ad hoc analysis of *Penn Central* . . . as opposed to *Loretto*'s per se approach." 271 F.3d at 855. In short, the en banc Ninth Circuit completely rejected the Fifth Circuit's taking analysis.

The decision of the court below not only conflicts with the Ninth Circuit's decision but also cannot be reconciled with this Court's instruction that only the most "extraordinary" and "rare" situations are subject to per se taking analysis. *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003, 1017-18 (1992). Recently, this Court reaffirmed its unwillingness to extend per se taking analysis beyond the context of physical taking cases. In *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Reg'l Planning Agency*, 122 S. Ct. 1465 (2002), the Court justified application of per se analysis to physical takings, but not other forms of taking, on the ground that "physical appropriations are relatively rare, easily identified, and usually represent a greater affront to individual property rights." *Id.* at 1479. The Court thrice repeated the admonition that "[t]he temptation to adopt what amount to per se rules in either direction must be resisted." *Id.* at 1478, 1480 n.23, 1489 (citation omitted).

The Fifth Circuit succumbed to that temptation here and analyzed Texas's IOLTA rules using a per se approach, even as it acknowledged that this Court has repeatedly declined to apply per se analysis to payments of money. *See Eastern Enters. v. Apfel*, 524 U.S. 498, 529-30 (1998) (plurality opinion); *United States v. Sperry Corp.*, 493 U.S. 52, 62 n.9 (1989); *Concrete Pipe & Prods. of Cal, Inc. v. Construction Laborers Pension Trust for S. Cal., Inc.*, 508 U.S. 602, 643-44 (1993); *Bowen v. Gilliard*, 483 U.S. 587, 606 (1987); *Connolly v. PBGC*, 475 U.S. 211, 224 (1986). The court of appeals incorrectly asserted that these cases all involved fees for government services. App., *infra*, 12a. In fact, only one of the five cases involved a fee for government services, and in that case (*Sperry*), the Court's *reason* for not applying per se analysis — that money is fungible — would have applied even if the case had not involved a fee-for-service. 493 U.S. at 62 n.9.

As noted by the seven judges who dissented from the denial of the petition for rehearing en banc, the panel's taking analysis is both "novel" and "far-reaching," with "exceptionally important constitutional and practical consequences" for Fifth Amendment jurisprudence. App., *infra*, 171a. The Fifth Circuit's approach threatens to transform a wide range of government activity into unconstitutional "confiscations" subject to per se analysis. Justice Souter has already cited withholding of income taxes as one example (*Id.* at 121a); another is the interest-free deposits that financial institutions are required to make with the Federal Reserve Banks. Indeed, most taxes are not fees

for particular services, and thus would be subject to attack as per se takings under the Fifth Circuit's ruling.[3]

Interest on IOLTA accounts could not exist without the client's principal, and therefore, as the Ninth Circuit held in its en banc opinion, "it is logically sound to analyze the two in combination for purposes of determining whether a taking of property occurred." 271 F.3d at 854. This Court, too, has warned against analysis of takings claims that defines the relevant universe of property interests too narrowly. *See, e.g., Andrus v. Allard*, 444 U.S. 51, 65-66 (1979) ("where an owner possesses a full 'bundle' of property rights the destruction of one 'strand' of the bundle is not a taking because the aggregate must be viewed in its entirety."); *Concrete Pipe & Prods.*, 508 U.S. at 643-44; *Penn Central*, 438 U.S. at 130-31. If there has not been "a total taking of the entire parcel," "then *Penn Central* [i]s the proper framework." *Tahoe-Sierra*, 122 S. Ct. at 1483-84.

Even if the relevant property is viewed (incorrectly, in Petitioners' view) as the interest alone, and even if the absence of any economic loss to the client is viewed (also incorrectly, in Petitioners' view) as irrelevant, the fact remains that the Texas IOLTA rules do *not* result in a "confiscatory" taking. The "bundle" of property rights includes the right to possess, use and enjoy the property, the right to exclude others from using it, and the right to sell it or give it away. *See, e.g., United States v. General Motors Corp.*, 323 U.S. 373, 378 (1945); *PruneYard Shopping Ctr. v. Robbins*, 447 U.S. 74, 82 (1980). The IOLTA rules do not deprive clients of all, or even many, of the "sticks" in this

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[3] Moreover, a taking may occur when government "takes property from A and gives it to B." *Calder v. Bull*, 3 U.S. 386, 388 (1798). Under the Fifth Circuit's approach to takings, a wide variety of other laws (*e.g.*, laws allowing banks to benefit from holding funds without paying interest) may be per se takings.

bundle. To the contrary, the property owner makes an independent decision — entirely separate and apart from IOLTA — to hand over money to a lawyer in circumstances in which the money cannot be made to earn interest for the client.

Once the client makes that decision, the rules of professional conduct — again separate and apart from the IOLTA rules — require the lawyer to deposit the client's money in a bank account. And the banking laws — also separate from the IOLTA rules — allow the bank to use the deposit in any way it sees fit, subject only to a contractual obligation to repay the principal on demand. In these circumstances, the client has no right to use or enjoy, let alone actually possess, any interest. Moreover, the client has no right to insist that the deposited funds "lie fallow," or to object if the bank decides to make loans or political or charitable contributions to particular recipients. As the Ninth Circuit concluded, IOLTA rules do not deprive plaintiffs of the right to control their property because they have already surrendered control. 271 F.3d at 863.

The situation in this case is similar to that in *PruneYard Shopping Center v. Robbins*, 447 U.S. 74 (1980), in which the Court rejected a taking claim on the ground that the owner had opened up the property to public use as a shopping center, and therefore could not object to its use for pamphleteering purposes. As then-Justice Rehnquist wrote for a unanimous court, even when "there has literally been a 'taking' of" the "right to exclude others," there is no "'taking' in the constitutional sense" if the value of the property is not unreasonably impaired. *Id.* at 82-83.

## II. THE FIFTH CIRCUIT'S HOLDING THAT CLAIMANTS WHO HAVE SUFFERED NO ECONOMIC LOSS ARE ENTITLED TO RELIEF UNDER THE JUST COMPENSATION CLAUSE CONFLICTS WITH THE NINTH CIRCUIT'S EN BANC DECISION AND THIS COURT'S PRECEDENTS.

In *Phillips*, this Court declined to express any "opinion as to the amount of 'just compensation,' if any, due respondents." App., *infra*, 114a. Four Justices joined an opinion that reviewed this Court's "just compensation" decisions and concluded that "a court presumably would look to the claimant's putative property interest as it was or would have been enjoyed in the absence of IOLTA," and "would measure any required compensation by the claimant's loss, not by the government's (or the public's) gain." *Id.* at 119a-20a. (citations omitted).

On remand, the district court made a factual finding, "based upon all the evidence before it, that Mr. Summers's loss is zero." *Id.* at 77a. Indeed, client Summers himself admitted that "he was no worse off because of IOLTA." *Id.* Applying the just compensation principles summarized in Justice Souter's opinion, the district court held that no "just compensation" was due, and therefore there was no violation of the Just Compensation Clause. On appeal to the Fifth Circuit Judge Wiener agreed that "when the owner's loss is zero, he is owed no compensation." *Id.* at 36a.

The panel majority disagreed. It held that "once a taking is found, the question becomes what amount of, not whether, just compensation is due." *Id.* at 15a. Having held that *some* compensation is due, the Fifth Circuit made no effort to determine the *amount* of compensation that is due to Mr. Summers. Instead, it considered only whether

Respondents are entitled to prospective declaratory and injunctive relief. *Id.* at 17a-25a.

The Fifth Circuit panel's ruling on just compensation conflicts with the Ninth Circuit's en banc decision in *WLF v. LFW* as well as decisions of this Court. The Ninth Circuit, relying on decisions of this Court cited by Justice Souter and Judge Wiener, held that the purpose of "just compensation" is to put "the owner of the condemned property in as good a position pecuniarily as if the property had not been taken" 271 F.3d at 862 (quoting *United States v. 564.54 Acres of Land*, 441 U.S. 506, 510 (1979) (quoting *Olson v. United States*, 292 U.S. 246, 255 (1934))). The Ninth Circuit also noted that, "without IOLTA, neither [plaintiff] would have earned interest on his principal . . ." *Id.* Thus, at most, IOLTA took away the plaintiffs' "opportunity to place the principal in a noninterest-bearing checking account." *Id.* at 863. That loss is of no economic value, and thus is "'not compensable under the Fifth Amendment.'" *Id.* at 864 (quoting *United States ex rel. Tenn. Valley Auth. v. Powelson*, 319 U.S. 266, 281 (1943)). Accordingly, the Ninth Circuit held that "even if the IOLTA program constituted a taking of [the plaintiffs'] private property, there would be no Fifth Amendment violation because the value of their just compensation is nil." *Id.*

On the just compensation issue, as on the taking issue, the Fifth Circuit's reasoning is unpersuasive. As Judge Wiener noted, it is a "constitutional truism" that "[t]he Fifth Amendment does not proscribe the taking of property; it proscribes taking without just compensation." *Id.* at 196 (quoting *Williamson County Reg'l Planning Comm'n v. Hamilton Bank*, 473 U.S. 172, 194 (1985)); *see also Suitum v. Tahoe Reg'l Planning* Agency, 520 U.S. 725, 734 (1997). This Court's opinions often emphasize this fundamental point by referring to the critical section of the Fifth Amendment as the "Just Compensation Clause" rather than

the "Taking Clause." *See, e.g., Suitum*, 520 U.S. at 734; *Williamson*, 473 U.S. at 195. If no compensation is due, there is no violation of the Just Compensation Clause.

The relevant question, for just compensation purposes, is "What has the owner lost? not, What has the taker gained?" *Boston Chamber of Commerce v. City of Boston*, 217 U.S. 189, 195 (1910). Where "nothing of value was taken," it follows that "nothing [is] recoverable as just compensation," even if "technically" there has been a "taking." *Marion & Rye Valley Ry. Co. v. United States*, 270 U.S. 280, 282 (1926).[4]

The Fifth Circuit's opinion fails to acknowledge these decisions, let alone explain how it is faithful to them. The opinion purports to rest on *Phillips*, but *Phillips* does not support the panel's ruling. (*See* App., *infra*, at 113a-14a) (expressing no opinion "as to the amount of 'just compensation,' if any, due"). The Fifth Circuit decision also cites *Loretto*, but that case does not support the panel's holding either. As Justice Souter noted, *Loretto* differs from this case in at least three ways: It (1) involved a permanent physical invasion of real property, (2) made no finding about the effect of the invasion on the value of the property, and (3) did not address the legal consequences of a finding that the value of the property had been enhanced. *Id.* at 120a. Indeed, *Loretto* stated that "[t]he issue of the amount of compensation that is due, on which we express no opinion, is a matter for the state courts to consider on remand." *Loretto*, 458 U.S. at 441. Moreover, the original Ninth Circuit panel decision in *WLF v. LFW* remanded to determine whether there was any compensable loss, and the dissenting judges on

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[4] *See also United States v. Pewee Coal Co.*, 341 U.S. 114, 674 (1951) (Reed, J., concurring) ("Where the owner's losses are what they would have been without the 'taking,' the owner has suffered no loss or damage for which compensation is due.").

the en banc court adopted that opinion. *See* 271 F.3d at 867. Thus, no judge of the Ninth Circuit agreed with the Fifth Circuit that a finding of a "taking" entails an automatic right to compensation.

In sum, there is no legal support for the Fifth Circuit's dismissal, as simply "not relevant," of the district court's finding of fact that under any applicable accounting method or economic analysis — including in-firm pooling, sub-accounting and net-benefit theory — the Respondents have suffered no loss. That ruling, like its ruling on the taking issue, represents a significant and unwarranted distortion of Just Compensation Clause jurisprudence. The Fifth Circuit distorted Just Compensation principles even further by holding that Respondents are entitled to injunctive or declaratory relief from a federal court without having sought compensation from the State, and without determining the amount of compensation that would be due.

## III. THE COURT SHOULD ALSO REVIEW THE FIFTH CIRCUIT'S HOLDING THAT THE TEXAS SUPREME COURT JUSTICES DO NOT HAVE LEGISLATIVE IMMUNITY.

This Court should also review the lower court's ruling that the Chief Justice and Justices of the Texas Supreme Court are not entitled to official immunity. In *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719 (1980), this Court recognized that when a state's highest court is enacting rules for the conduct of the state bar, it is acting in a legislative capacity and entitled to legislative immunity for those actions. *Id.* at 731-73. In contrast, when a State's highest court exercises independent enforcement authority to initiate proceedings against attorneys, it may be subject to a suit for declaratory or injunctive relief. *Id.* at 734-36.

In this case, the Fifth Circuit held that a rule providing for automatic suspension without any direct involvement of the Justices is sufficient to subject them to a suit for declaratory and injunctive relief. *See* App., *infra*, 26a-27a. This holding renders meaningless the distinction established by this Court between legislative powers and enforcement powers. Virtually every state high court has the inherent power to discipline attorneys, and all rules enacted by those courts subject attorneys to disciplinary actions for failure to comply, although most disciplinary actions do not directly involve those courts. Thus, all state high courts would be subject to suit over any rule they promulgated without regard to their direct involvement in enforcement of that rule, virtually nullifying their legislative immunity.

Respondents seek in part to enjoin the Justices from "adopting any rules that purport to require attorneys, as a condition for practicing law in Texas, to handle client trust funds in a manner designed to ensure that interest on those funds will accrue to anyone not designated by the client." App., *infra*, 16a. The requested relief falls squarely within the Justices' legislative prerogative, and the relief sought impermissibly restricts their legislative authority. Accordingly, the Fifth Circuit's denial of the Justices' claim of official immunity warrants review as an additional question presented.[5]

## IV. THIS CASE SHOULD BE CONSOLIDATED WITH *WLF v. LFW.*

This Court has already granted review in *WLF v. LFW*. Ordinarily, the court would simply hold the petition in

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[5] Petitioners have not claimed that TEAJF is entitled to immunity. Thus, according immunity to the Chief Justice and Justices of the Texas Supreme Court would not prevent Respondents from obtaining effective relief.

this case until it issues a decision in *WLF v. LFW*. For several reasons, however, the Court should grant review in this case as well as in *WLF v. LFW* and consider the two cases together.

*First*, there has been a trial on the merits in this case, and the district court has made findings of fact. In *WLF v. LFW*, in contrast, there has been no trial, and thus there is no trial record and no findings of fact. Indeed, that case has not even been before a district court since prior to this Court's decision in *Phillips*. This Court has often recognized that a complete trial record may be of considerable assistance in resolving legal issues. *See United States v. International Union United Auto.*, 352 U.S. 537, 542 (1957); *see also Dombrowski v. Eastland*, 387 U.S. 82, 84 (1967); *Kennedy v. Silas Mason Co.*, 334 U.S. 249, 257 (1948). The recent *Lake Tahoe* case underscored the usefulness of a trial record in considering the merits of a taking issue. 122 S. Ct. 1465. In this case in particular, a trial record and the district court's findings of fact are likely to assist the Court in evaluating plaintiff's claims that his property has been "taken" against the background of the actual workings of the Texas IOLTA program and the banking alternatives available to lawyers and their clients both with and without IOLTA.

*Second*, the Texas TEAJF program, like most of the country's IOLTA programs, applies only to client funds held by lawyers. In contrast, the Washington program involves non-lawyer "Limited Practice Officers."[6]

*Third*, the Court is already familiar with this case. Having specified the issues remaining open on remand, the Court can now review how the district court and court of appeals addressed those issues. In addition, a second

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[6] "Limited Practice Officers" are nonlawyers licensed to select, prepare, and complete real estate and personal property transactions.

decision of this Court in the same case, concerning the same state program, may provide an added degree of continuity and guidance to those who must abide by the Court's decision.

If the Court wishes to grant the petition in this case, Petitioners stand ready to prepare and file briefs on the merits in less than the usual time allowed, or to make other adjustments to the usual schedule to allow this case to be argued together with *WLF v. LFW.*

## CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 00-50139

WASHINGTON LEGAL FOUNDATION; William R. Summers; and Michael J. Mazzone,

Plaintiffs-Appellants,

v.

TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; Richard Tate, Chairman, Texas Equal Access to Justice Foundation; Thomas R. Phillips, Chief Justice; Nathan L. Hecht, Justice; Craig Enoch, Justice; James A. Baker, Justice; Priscilla R. Owens, Justice; Greg Abbott, Justice; Deborah Hankinson, Justice; Harriet O'Neill, Justice; Supreme Court

Defendants-Appellees.

October 15, 2001

Appeal from the United States District Court for the Western District of Texas.

Before WIENER, BARKSDALE, and EMILIO M. GARZA, Circuit Judges.

RHESA HAWKINS BARKSDALE, Circuit Judge:

The Supreme Court having held in this case that, for purposes of the Takings Clause of the Fifth Amendment, interest earned on client-funds deposited in demand accounts pursuant to the Texas Interest on Lawyers Trust Accounts (IOLTA) program is the "private property" of the client, *Phillips v. Washington Legal Foundation,* 524 U.S. 156, 160, 172, 118 S.Ct. 1925, 141 L.Ed.2d 174 (1998), and the Court having remanded this case for consideration, *inter alia,* of two other subparts of the Takings Clause (whether there has been a "taking" and, if so, what "just compensation", if any, is due, *id.* at 172, 118 S.Ct. 1925), and the district court, following a bench trial on remand, having concluded, *inter alia,* there was neither a compensable loss nor a taking, the principal issues at hand are: whether there can be a taking when, without the cost-savings provided by the IOLTA program, client-funds would not earn "net" interest; and whether, even if there is a taking, prospective injunctive relief can be a remedy.

Because we hold that the Fifth Amendment is violated, we need not reach Appellants' claim that the IOLTA program violates the First Amendment as well. REVERSED and REMANDED.

I.

The requisite underlying facts have been fully discussed in prior opinions by the Supreme Court and our court. *See Phillips v. Washington Legal Found.,* 524 U.S. 156, 118 S.Ct. 1925, 141 L.Ed.2d 174 (1998); *Washington Legal Found. v. Texas Equal Access to Justice Found.,* 94 F.3d 996 (5th Cir.1996). They are restated here, together with pertinent new facts.

When attorneys hold their clients' funds, Texas ethical rules require placing those funds in a trust account that permits withdrawal on demand. Tex. Disciplinary Rules of Professional Conduct, Art. 10, § 9, Rule 1.14(a). Those rules allow attorneys to aggregate client-funds in a single

trust account, but, of course, prohibit attorneys from commingling their money with the trust fund. *Id.* Prior to 1980, because federal law prohibited banks from paying interest on demand accounts, these accounts were, in effect, interest-free loans to the banks. *See* S.Rep. No. 96-368, at 5 (1980), reprinted in 1980 U.S.C.C.A.N. 236, 240.

In 1980, Congress enacted legislation that allowed negotiable order of withdrawal (NOW) accounts. *See* Depository Institutions Deregulation and Monetary Control Act of 1980, 94 Stat. 132, 146 (codified as amended at 12 U.S.C. § 1832). In general, NOW accounts allow attorneys to pool client-funds in an interest-bearing trust account.[1]

The creation of NOW accounts led to the creation of IOLTA programs. When either the amount of a client's funds to be held is nominal or the period of time for which the funds will be held is brief, a NOW account for such client-funds is not feasible, because the cost of maintaining the account is greater than the interest the client would have earned (*no* "net interest"). As discussed *infra,* such costs are those incurred not only by the bank, but also by the attorney. In this situation, the trust accounts are – as they were formerly – interest-free loans to the banks. IOLTA programs transfer this benefit from the bank to legal providers for the indigent. Based on the assumption – later held erroneous in *Phillips* – that the interest generated was not the client's property, the American Bar Association's Standing Committee on Ethics and Professional Responsibility opined

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[1] None of the funds may belong to a for-profit corporation or partnership. 12 U.S.C. § 1832(a)(2). ***But see*** Letter from Federal Reserve Board General Counsel Michael Bradfield to Donald Middlebrooks (15 Oct. 1981), reprinted in Middlebrooks, *The Interest on Trust Accounts Program: Mechanics of its Operation,* 56 FLA. B.J. 115, 117 (Feb.1982) (concluding corporate funds may be held in NOW accounts *if* charitable organizations have exclusive right to interest generated by funds).

that IOLTA programs are ethical. *See* ABA Comm. on Ethics and Prof'l Responsibility, Formal Op. 348 (1982).

The Texas Supreme Court created its IOLTA program in 1984. The program was voluntary, permitting an attorney to place client-funds that were "nominal in amount" or "reasonably anticipated to be held for a short period of time" in an unsegregrated, interest-bearing bank account (an IOLTA account), the interest on which was paid to the Texas Equal Access to Justice Foundation (TEAJF), a non-profit corporation created by the Texas Supreme Court. *See* TEX. GOV'T CODE ANN. tit. 2, subtit. G, app. A, art. 11 §§ 6-7 (1987). TEAJF manages the interest earned from the IOLTA accounts and distributes it to non-profit organizations that "have as a primary purpose the delivery of legal services to low income persons", with the exception that funds may not be used to finance class actions or to lobby on behalf of a political candidate or issue. *See* TEXAS RULES OF COURT–STATE, Rules Governing the Operation of the Texas Equal Access to Justice Program [TEAJF rule] rule 10, 15 (West 1996).

Texas' voluntary IOLTA program generated only $1 million annually. Therefore, in 1988, following the lead of several other States and the recommendation of the American Bar Association, the Texas Supreme Court made mandatory attorney participation in the IOLTA program.

> An attorney . . . receiving in the course of the practice of law . . . client funds that are *nominal in amount* or are *reasonably anticipated to be held for a short period* of time, *shall* establish and maintain a separate interest-bearing demand account at a financial institution and *shall* deposit in the account all those client funds.

TEX. GOV'T CODE ANN. tit. 2, subtit. G, app. A, art. 11 § 5 (West Supp.1995) (emphasis added). The rules define

which funds are "nominal in amount" and/or "held for a short period of time". They state that a client's funds may be deposited in an IOLTA account only if the attorney holding the funds determines they

> could *not* reasonably be expected to earn interest for the client *or* if the interest which might be earned on such funds is *not likely* to be sufficient to *offset the cost* of establishing and maintaining the account, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain interest on such funds for the client.

TEAJF rule 6 (emphasis added).[2]

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[2] When Phillips was decided, the parties agreed that the portion of then TEAJF rule 6 prohibiting attorneys from pooling clients' funds in one account in an effort to generate net interest for the clients was not enforced. *Phillips*, 524 U.S. at 169, 118 S.Ct. 1925. That portion was omitted in the January 1999 revision to the TEAJF rules. TEAJF rule 6.

Consistent with the following ruling in *Phillips*, this rule-change does not affect our analysis concerning whether there has been a taking.

Whether client funds held in IOLTA accounts could generate net interest [for a client] is a matter of some dispute. As written [(prior to the above-referenced January 1999 TEAJF rules-revision)], the Texas IOLTA program requires the calculation as to net interest to be made "without regard to funds of other clients which may be held by the attorney." [TEAJF] Rule 6. This provision would deny to an attorney the traditional practice of pooling funds of several clients in one account, a practice which *might* produce net interest when opening an account for each client would *not*. But in the District Court, petitioners [(Appellees here)] agreed that this portion of the rule was *not* to be enforced, and that an attorney could make the necessary calculation on the basis of pooled accounts. Petitioners made a similar concession during oral argument here. Tr. of Oral Arg. 13-16. We accept this concession but find that it does *not* avail petitioners. *Phillips*, 524 U.S. at 169, 118 S.Ct. 1925 (emphasis added).

The January 1999 guidelines to the TEAJF rules provide attorneys "should consider all costs associated with such an account" in determining whether a client's funds are suitable for deposit in the program. But, W. Frank Newton, past chair of TEAJF and member of its board of directors, testified that attorneys may disregard their overhead costs. (As Appellees note, the guidelines have been revised – approximately when the trial on remand was held in September 1999 – to provide that attorneys may consider all costs associated with such an account.)

Attorneys must review periodically whether changed circumstances require removing a client's funds from an IOLTA account. TEAJF rule 6. Along this line, if an attorney determines funds were erroneously placed in an IOLTA account, he must notify TEAJF and seek a refund of the interest earned.

The mandatory IOLTA program generated much more revenue than its predecessor. Recent earnings approximate over $5 million annually.

As noted, Texas' IOLTA program was made mandatory in 1988. In 1994, Michael J. Mazzone, a Texas attorney who regularly places client-funds in an IOLTA account,[3] William R. Summers, a Texas citizen who currently has funds in an IOLTA account, and Washington Legal Foundation, a public interest law firm with members similarly situated to Mazzone and Summers (Appellants), filed this action against the Texas IOLTA program, naming as defendants TEAJF, TEAJF's chairman, and the nine Justices of the Texas Supreme Court (Appellees). Appellants

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[3] Mazzone's unopposed 29 May 2001 motion (post-oral argument) to dismiss his appeal was denied. *See* Fed. R.App. P. 42(b) ("An appeal may be dismissed on the appellant's motion on terms agreed to by the parties or fixed by the court.").

claimed: the IOLTA program impermissibly takes interest earned from client-funds, in violation of the Fifth Amendment; and the program forces Appellants to support speech they find offensive, in violation of the First Amendment. Appellants sought monetary reimbursement, as well as declaratory and injunctive relief.

The district court granted Appellees' motion for summary judgment, concluding clients lacked property rights in the interest generated by their funds. *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 873 F.Supp. 1, 7 (W.D.Tex.1995). But, through an opinion authored by the late Judge John Minor Wisdom, our court reversed in part, holding the interest was the clients' property. *Washington Legal Found.*, 94 F.3d at 1000. On the other hand, our court affirmed the district court's conclusion that Appellees have Eleventh Amendment immunity from the monetary-restitution claim. *Id.* at 1005.

The Supreme Court granted certiorari, limiting its review to: "Is interest earned on client trust funds held by lawyers in IOLTA accounts a property interest of the client or lawyer, cognizable under the Fifth Amendment of the United States Constitution, *despite the fundamental precept of IOLTA that such funds, absent the IOLTA program, could [not] earn interest for the client [or] lawyer*". *Phillips v. Washington Legal Found.*, 521 U.S. 1117, 117 S.Ct. 2535, 138 L.Ed.2d 1011 (1997) (emphasis added). In June 1998, the Court affirmed, stating the issue to be "whether interest earned on client-funds held in IOLTA accounts is 'private property' of either the client or the attorney for purposes of the Takings Clause", and holding the interest is the property of the client. *Phillips*, 524 U.S. at 160, 118 S.Ct. 1925. In the light of its "hold[ing] that the interest income generated by funds held in IOLTA accounts is the 'private property' of the owner of the principal [,the client,]", *id.* at 172, 118 S.Ct. 1925, the Court remanded for further proceedings, including

a determination of whether the interest has been "taken" by the State and the amount of "just compensation", if any, due. *Id.*

A bench trial was held in September 1999. In January 2000, the district court granted the Texas Supreme Court Justices' motion for judgment on the pleadings, holding the Justices are legislatively immune from suit. *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 86 F.Supp.2d 617, 624 (W.D.Tex.2000). Later that month, the court dismissed the remaining claims, concluding the IOLTA program was not violative of either the Fifth or First Amendments. *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 86 F.Supp.2d 624, 636, 643 (W.D.Tex.2000).

Regarding the taking claim, the court concluded that the "just compensation" subpart of the Takings Clause had not been violated; this was premised on its conclusion that Appellants failed to show an identifiable compensable loss because a client's IOLTA-deposit funds cannot generate "net interest" without the IOLTA program. *Id.* at 643. Again, by "net interest", the court meant interest in excess of the costs associated with establishing and maintaining an interest-bearing demand account. *Id.* at 628 (citing TEAJF rule 6); *see also* TEAJF rule 4B. In the alternative, and applying the ad hoc analysis referenced *infra,* the court concluded there had been no taking. *Id.* at 643-47.

II.

The district court's conclusions of law are reviewed *de novo;* its findings of fact, for clear error. *E.g., Dunbar Med. Sys., Inc. v. Gammex Inc.*, 216 F.3d 441, 448 (5th Cir.2000). Of course, whether public interests are served by Texas' IOLTA program is not the question. Instead, at issue is the constitutionality *vel non* of the program. Because Appellants' Fifth Amendment claim has merit, we do not reach their claim that the IOLTA program violates their First

Amendment rights by forcing them to finance speech they find objectionable.

The Takings Clause of the Fifth Amendment, made applicable to the States through the Fourteenth, provides: "nor shall private property be taken for public use, without just compensation". U.S. CONST. amend. V; *Phillips,* 524 U.S. at 163-64, 118 S.Ct. 1925. Appellants have met their burden of demonstrating the existence of a property interest. *Id.* at 172, 118 S.Ct. 1925. And, there is no dispute that "private property" has been allocated "for public use". Therefore, has there been a "taking"? If so, what "just compensation", if any, is due?

A.

For determining whether there has been a taking, Appellants urge use of the per se analysis; Appellees, the ad hoc inquiry set forth in *Penn Central Transportation Co. v. City of New York,* 438 U.S. 104, 124, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978) (three factors of "particular significance": economic impact of regulation; extent of interference with distinct investment-backed expectations; and character of governmental action).

On remand, the district court first rejected using the per se analysis, and then applied the ad hoc method. *Washington Legal Found.,* 86 F.Supp.2d at 643-47. We conclude, however, that *Phillips,* and *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980), and *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982), cases the *Phillips* Court relied upon in

reaching its property interest holding, compel applying the per se analysis.[4]

*Webb's,* 449 U.S. at 155-56, 101 S.Ct. 446, the case most factually similar to the one at hand, involved a state statute pursuant to which, in addition to charging a fee for the clerk's services in receiving an interpleader fund into the registry of its court, a county took the interest accruing on that deposited fund. Citing *Penn Central,* but not engaging in the ad hoc analysis articulated in it, the Court first noted it "has been permissive in upholding" governmental action that denies a property owner the full use of his property, if that action promotes the general welfare. *Id.* at 163, 101 S.Ct. 446.

> [For the governmental action at issue in *Webb's*], however, [the government] has not merely adjusted the benefits and burdens of economic life to promote the common good. Rather, the exaction is a *forced contribution* to general governmental revenues, and it is not reasonably related to the costs of using the courts.

*Id.* (emphasis added; internal quotation marks and citation omitted). The exaction was found similar to that in *United States v. Causby,* 328 U.S. 256, 66 S.Ct. 1062, 90 L.Ed. 1206 (1946): "The county's appropriation of the beneficial use of the fund is analogous to the appropriation of the use of private property in . . . *Causby*." *Webb's*, 449 U.S. at 163-64, 101 S.Ct. 446.

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[4] Likewise, in a similar IOLTA case, a panel of the Ninth Circuit recently applied the per se analysis. *Washington Legal Found. v. Legal Found. of Wash.*, 236 F.3d 1097, 1111 (9th Cir.2001). But, rehearing en banc was granted on 9 May 2001. *Washington Legal Found. v. Legal Found. of Wash.*, 248 F.3d 1201 (9th Cir.2001).

In *Causby*, 328 U.S. at 258-59, 66 S.Ct. 1062, the Government's use of air space above private property as part of the flight plan for military aircraft was held to be a taking: the appropriation destroyed the use of the land as a chicken farm. *Causby* was decided *before* the per se takings analysis was articulated. But, *Lucas v. South Carolina Coastal Council,* 505 U.S. 1003, 1015, 112 S.Ct. 2886, 120 L.Ed.2d 798 (1992), classified *Causby* as involving a "physical invasion of property", one of "at least two distinct categories of regulatory action . . . compensable without case-specific inquiry into the public interest advanced in support of the restraint".[5] Continuing the discussion of the per se analysis, and of great significance to the taking issue presented by the case at hand, the Court stated:

> In general (at least with regard to permanent invasions), no matter how minute the intrusion, and no matter how weighty the public purpose behind it, we have required compensation. For example, in *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982), we determined that New York's law requiring landlords to allow television cable companies to emplace cable facilities in their apartment buildings constituted a taking, *id.*, at 435-40, 102 S.Ct. 3164, even though the facilities occupied at most only 1 1/2 cubic feet of the landlords' property, see *id.*, at 438, n. 16, 102 S.Ct. 3164. *See also United States v. Causby*, 328 U.S. 256, 265, and n. 10, 66 S.Ct. 1062, 90 L.Ed. 1206 (1946) (physical

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[5] The second type listed was "where regulation denies all economically beneficial or productive use of land". *Lucas*, 505 U.S. at 1015, 112 S.Ct. 2886.

> invasions of airspace); *cf. Kaiser Aetna v. United States*, 444 U.S. 164, 100 S.Ct. 383, 62 L.Ed.2d 332 (1979) (imposition of navigational servitude upon private marina).

*Id.* at 1015, 112 S.Ct. 2886.

Appellees maintain the Court has repeatedly rejected governmental appropriation of money being subjected to the per se analysis. They rely, however, on cases where the government provided a service and charged a reasonable fee for that service. *See, e.g., United States v. Sperry Corp.*, 493 U.S. 52, 110 S.Ct. 387, 107 L.Ed.2d 290 (1989) (upholding imposition of reasonable fee for use of Iran-United States Claims Tribunal). As *Phillips* determined, the case at hand is not such a case:

> This would be a different case if the interest income generated by IOLTA accounts was transferred to the State *as payment for services rendered by the State.* Our holding does *not* prohibit a State from imposing reasonable fees it incurs in generating and allocating interest income. But here the State does not, indeed cannot, argue that its *confiscation* of [a client's] interest income amounts to a fee for services performed.

*Phillips,* 524 U.S. at 171, 118 S.Ct. 1925 (emphasis added; internal quotation marks and citations omitted). Moreover, the analysis in *Webb's* dispels any assertion that the per se test applies solely to governmental appropriation of real property.

Appellees also emphasize the district court's finding, 86 F.Supp.2d at 643, that, absent the IOLTA program, net interest could not have been generated on Appellant Summers' funds. But, as referenced earlier, the Court concluded in *Loretto,* 458 U.S. at 434-35, 102 S.Ct. 3164,

that a government's permanent physical occupation of property constitutes a per se taking, regardless of the economic impact on the owner. Even more to the point, as stated in *Phillips,* 524 U.S. at 170, 118 S.Ct. 1925: "The government may not seize rents received by the owner of a building simply because it can prove that the costs incurred in collecting the rents exceed the amount collected". Along this line, *Phillips* made clear that a client's rights to possess, control, and dispose of the interest earned on his funds are valuable rights, regardless of whether the interest has economic value. *Id.*[6]

As our court has already noted for the case at hand, in order to prevail on their taking claim, Appellants must demonstrate the taking was against the will of the property owner. *Washington Legal Found.,* 94 F.3d at 1004. Appellant Summers testified he objected to his interest being taken to support Texas' IOLTA program. However, he had no choice. IOLTA programs are structured so that they satisfy Internal Revenue Service ruling 81-209, by which the IRS agrees not to tax clients on the interest generated by their funds in IOLTA accounts and paid to TEAJF if they have no control over whether to participate in the program. *See* Rev. Rul. 81-209, 1981-2 C.B. 16, 1981 WL 165692; *Phillips*, 524 U.S. at 162, 118 S.Ct. 1925; *Washington Legal Found.*, 94 F.3d at 1003. Clients have no choice whether to participate because attorney participation in Texas' IOLTA program is mandatory. Therefore, a client cannot avoid the

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[6] The dissent at 198 maintains, erroneously, that we ignore the district court's factual findings. Instead, we conclude, in the light of *Phillips* and *Loretto,* that they are not relevant. Pursuant to these cases, the economic impact on the owner is a non-factor in the takings analysis. *See* note 10 *infra.*

appropriation of his interest by selecting an attorney who elects *not* to participate.[7]

In reality, the linchpin for this case has already been inserted by the Supreme Court: "interest income generated by funds held in IOLTA accounts is the 'private property' of the owner of the principal" – the client. *Phillips,* 524 U.S. at

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[7] Subsequent to oral argument, we directed the parties to file supplemental briefs on whether this case is resolved by *Paulsen v. State Bar of Tex.*, 2001 WL 23180 (Tex.App.–Austin 11 Jan. 2001), *withdrawn on reh'g,* 2001 WL 300142 (Tex.App.–Austin 29 Mar. 2001), interpreting Tex. Disciplinary Rules of Professional Conduct, Art. 10, § 9, Rule 1.14(a); and TEAJF rules 21 and 22. In *Paulsen,* an attorney appealed the State Bar's refusal to grant him an exemption from IOLTA participation. In the course of rejecting that challenge, the Texas Court of Appeals, *in its original opinion,* stated:

> [T]hese rules permit lawyers to make full disclosure to clients regarding the use of IOLTA accounts and clients' property interest therein. . . . [L]awyers must invest client funds as directed by their clients. If a client directs his lawyer to withdraw his funds from an IOLTA account, the lawyer should do so and inform the Bar that he takes such action at his client's insistence. The IOLTA Rules provide that lawyers cannot be compelled to take any action in violation of the Disciplinary Rules. Because client funds are unquestionably client property, investing such funds in a manner contrary to a client's instructions would be a violation of the Disciplinary Rules and the lawyer's fiduciary duties.

*Id.* 2001 WL 23180, at *10. Obviously, the quoted language could be construed as interpreting the State Bar and TEAJF rules as making client participation in IOLTA *voluntary,* rather than *mandatory.*

In their supplemental briefs, the parties agreed, albeit for different reasons, that the original *Paulsen* opinion did *not* resolve the case at hand. In any event, subsequent to our requesting supplemental briefs, the opinion was revised to delete the above quoted language. *See Paulsen,* 2001 WL 300142, at *10.

172, 118 S.Ct. 1925.[8] And, because the State has permanently appropriated Appellant Summers' interest income against his will, instead of merely regulating its use, there is a per se taking. *Compare Loretto,* 458 U.S. at 432 & n. 9, 102 S.Ct. 3164, with *Penn Central,* 438 U.S. at 124, 98 S.Ct. 2646.

> Once the fact of occupation is shown, . . . a court should consider the *extent* of the occupation as one relevant factor in determining the compensation due. For that reason, . . . there is less need to consider the extent of the occupation in determining whether there is a taking in the first instance.

*Loretto,* 458 U.S. at 437-38, 102 S.Ct. 3164 (emphasis in original; footnote omitted). In other words, once a taking is found, the question becomes what amount of, not whether, just compensation is due. *Id.* at 441, 102 S.Ct. 3164; *see also First English Evangelical Lutheran Church of Glendale v. County of Los Angeles, Cal.,* 482 U.S. 304, 314, 107 S.Ct. 2378, 96 L.Ed.2d 250 (1987) (Takings Clause "does not prohibit the taking of private property, but instead places a condition on the exercise of that power"); *Monongahela Navigation Co. v. United States,* 148 U.S. 312, 336, 13 S.Ct. 622, 37 L.Ed. 463 (1893) (government "can take only on payment of just compensation").[9] Again, as explained in

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[8] Appellees request certifying to the Texas Supreme Court the question of whether a client has any property right in a Texas IOLTA account. *Phillips* has answered that question in the affirmative.

It is well to remember that a "taking" is distinct from "just compensation".

[9] The dissent, thus, creates an anomaly by assuming at 198 there has been a "taking", yet concluding at 199 that, because there can be no "just compensation" for it, the taking is not unconstitutional. Contrary to the

(continued...)

*Phillips,* 524 U.S. at 170, 118 S.Ct. 1925, there can be a compensable taking of a property right "even when infringement of that right arguably increase[s] the market value of the property at issue".[10]

B.

Originally, Appellants sought not only reimbursement of the earned interest, but also the following declaratory and injunctive relief: (1) declaring void rules requiring attorneys to place client-funds in IOLTA accounts; (2) enjoining TEAJF from both compiling lists of attorneys who fail to comply with IOLTA and transmitting those lists to the State Bar; and (3) enjoining the Justices of the Texas Supreme Court from (a) adopting any rules that purport to require attorneys, as a condition for practicing law in Texas, to handle client-funds in a manner designed to ensure that interest on those funds will accrue to anyone not designated by the client, and (b) taking disciplinary action against any attorney for failing to deposit client-funds in an IOLTA account.

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(footnote continued)

dissent's perception of the taking, in play is a "physical taking [ ] of tangible property", *Dissent* at 203.

[10] For the reasons given *supra,* that there has been a "taking" is not contingent on whether the client would have had "net interest" without the IOLTA program. Nevertheless, Appellants posit the following: deposits in demand accounts earn some interest, albeit at a low rate; the related costs are what preclude net interest; and it is the client's prerogative to incur those costs related to his earned interest on his principal even though, by doing so, it would probably result in a loss to the client.

Restated, Appellants urge that the earned interest must be segregated from the costs; that, notwithstanding those costs, the client has earned interest on his principal, and it is for him (his right) to decide how to use that interest. As stated, in the light of our foregoing analysis, it is not necessary to consider this contention.

But, as noted, our court has affirmed the district court's holding that the Eleventh Amendment bars Appellants' monetary-reimbursement claim. *Washington Legal Found.*, 94 F.3d at 1005. Therefore, Appellants now seek only prospective declaratory and injunctive relief.

1.

Following the remand by the Supreme Court, Appellees, for the first time, took the position that injunctive relief is not available, claiming: the only remedy for an unconstitutional taking is just compensation; and Appellants should have sought it in state court. Although Appellees maintain that position here, they do not strenuously urge it as a basis for affirmance.

The district court did not reach this issue. Instead, it noted that, although Appellants were seeking only declaratory and injunctive relief, "they must still prove that a taking occurred 'without just compensation' in order to establish a violation of the Fifth Amendment, which is a prerequisite to relief". *Washington Legal Found.*, 86 F.Supp.2d at 643 n. 8.

a.

Perhaps the district court did not rule on this remedy issue because, in the prior appeal to our court, our court had stated: "[Appellees] *concede* that they are *subject to* [Appellants'] prospective injunction claims". *Washington Legal Found.*, 94 F.3d at 1005 (emphasis added).[11]

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[11] The dissent at 196-98 posits erroneously that we hold Appellees conceded Appellants were "entitled" to equitable relief. Obviously, being "subject to" a claim is not the same as the party opposite being "entitled" to the corresponding requested relief. In any event, Appellees' concession in the prior appeal (that they were "subject to" Appellants' prospective injunction claims) is inconsistent with their position in this (continued...)

Appellees are bound by that concession; they cannot now take an inconsistent position. *See Jett v. Zink,* 474 F.2d 149, 154-55 (5th Cir.) (party who argued on first appeal that action was *in personam* precluded from arguing on second appeal that action was *quasi in rem* ), *cert. denied,* 414 U.S. 854, 94 S.Ct. 153, 38 L.Ed.2d 104 (1973). *Cf. United States v. Morris,* 79 F.3d 409, 411 (5th Cir.1996) (in criminal case, refusing to allow Government to take position on appeal inconsistent with that in district court); *Gregory v. Missouri Pacific R.R. Co.,* 32 F.3d 160, 164-65 (5th Cir.1994) (although "appellee generally may urge in support of a judgment any matter appearing in the record", it "cannot take one position before the district court and then take an inconsistent position" on appeal).

b.

In the alternative, Appellees' injunctive-and-declaratory-relief-unavailable-contention fails. Nevertheless, the contention has some support.

In *Duke Power Co. v. Carolina Environmental Study Group, Inc.,* 438 U.S. 59, 98 S.Ct. 2620, 57 L.Ed.2d 595 (1978), individuals living near planned nuclear power facilities sought a declaration that the Price-Anderson Act, 42 U.S.C. § 2210, was unconstitutional. That Act imposed a limitation on liability for nuclear accidents resulting from the operation of private nuclear power plants licensed by the United States. Among other things, one claim was "in the event of a nuclear accident, their property would be 'taken' without any assurance of just compensation". *Id.* at 69, 98 S.Ct. 2620. Then Justice Rehnquist, in his separate opinion concurring in the judgment, maintained that the taking claim

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(footnote continued)

appeal that equitable relief is not available, that, instead, the only remedy for an unconstitutional taking is just compensation.

could be adjudicated only in the Court of Claims under the Tucker Act, 28 U.S.C. § 1491 (granting jurisdiction to Court of Federal Claims to render judgment on claims against the United States founded on, *inter alia,* the Constitution). *Id.* at 101-02 & n. 4, 98 S.Ct. 2620 (Rehnquist, J., concurring). The majority held otherwise:

> Appellees are not seeking compensation for a taking, a claim properly brought in the Court of Claims, but are now requesting a declaratory judgment that *since the Price-Anderson Act does not provide advance assurance of adequate compensation in the event of a taking,* it is unconstitutional.... While the Declaratory Judgment Act does *not* expand our jurisdiction, it expands the scope of available remedies. Here it allows individuals threatened with a taking to seek a declaration of the constitutionality of the disputed governmental action before potentially *uncompensable* damages are sustained.

*Id.* at 71 n. 15, 98 S.Ct. 2620 (emphasis added).

Six years later, in *Ruckelshaus v. Monsanto Co.,* 467 U.S. 986, 104 S.Ct. 2862, 81 L.Ed.2d 815 (1984), the Court considered Monsanto's request for injunctive and declaratory relief, based on its claim that the data-disclosure and data-consideration provisions of the Federal Insecticide, Fungicide, and Rodenticide Act (FIFRA), 7 U.S.C. § 136, *et seq.,* effected a taking of its property (trade secrets) without just compensation. The Court stated: "Equitable relief is not available to enjoin an alleged taking of private property for a public use, duly authorized by law, when a suit for compensation can be brought against the sovereign subsequent to the taking". *Id.* at 1016, 104 S.Ct. 2862 (footnote omitted). The Court held: because Congress, in

FIFRA, had not expressly withdrawn jurisdiction under the Tucker Act, a Tucker Act remedy was available for any uncompensated taking. *Id.* at 1017-19, 104 S.Ct. 2862. Accordingly, Monsanto's challenges to the constitutionality of FIFRA were held not ripe for resolution. *Id.* at 1019, 104 S.Ct. 2862.

*Monsanto* did not overrule *Duke Power.* In fact, *Monsanto* cited *Duke Power* in support of the conclusion that Monsanto's claims were not ripe. *Id.* at 1021, 104 S.Ct. 2862. *See also Preseault v. ICC,* 494 U.S. 1, 11, 110 S.Ct. 914, 108 L.Ed.2d 1 (1990) (taking claim against United States premature until property owner has availed itself of process provided by Tucker Act).

A year after *Monsanto* was decided, the Court applied its ripeness doctrine in a case in which the owner of property being developed as a residential subdivision claimed a county planning commission's application of zoning laws and regulations constituted a taking of its property. *Williamson County Reg'l Planning Comm'n v. Hamilton Bank,* 473 U.S. 172, 195, 105 S.Ct. 3108, 87 L.Ed.2d 126 (1985). The Court held that, because the property owner had "not yet obtained a final decision regarding the application of the zoning ordinance and subdivision regulations to its property, nor utilized the procedures [state law] provides for obtaining just compensation", its claim was "not ripe". *Id.* at 186, 105 S.Ct. 3108.

The Court explained that the Fifth Amendment does not "require that just compensation be paid in advance of, or contemporaneously with, the taking; all that is required is that a reasonable, certain and adequate provision for obtaining compensation exist at the time of the taking". *Id.* at 194, 105 S.Ct. 3108 (internal quotation marks omitted; citing *Monsanto* ). As is the case with taking claims against the United States, which are premature until the property owner has sought just compensation under the Tucker Act,

"if a State provides an adequate procedure for seeking just compensation, the property owner cannot claim a violation of the Just Compensation Clause until it has used the procedure and been denied just compensation". *Id.* at 195, 105 S.Ct. 3108.

Following *Monsanto,* the Ninth Circuit held that the "exclusive remedy" for a taking claim against the United States is "a suit for money damages under the Tucker Act"; therefore, neither declaratory nor injunctive relief is available. *Clouser v. Espy,* 42 F.3d 1522, 1539 (9th Cir.1994) (citing *Monsanto* ), *cert. denied,* 515 U.S. 1141, 115 S.Ct. 2577, 132 L.Ed.2d 827 (1995). *See also Rose Acre Farms, Inc. v. Madigan,* 956 F.2d 670, 673-74 (7th Cir.) (reversing grant of injunctive relief against enforcement of federal regulation because of availability of just compensation under Tucker Act (citing *Monsanto* and *Preseault* )), *cert. denied,* 506 U.S. 820, 113 S.Ct. 68, 121 L.Ed.2d 34 (1992).

Other circuits have held otherwise. *See Student Loan Mktg. Ass'n v. Riley,* 104 F.3d 397, 402 (D.C.Cir.) (entertaining declaratory relief request where alleged taking involved "straightforward mandate[ ]of cash payment to the government"), *cert. denied,* 522 U.S. 913, 118 S.Ct. 295, 139 L.Ed.2d 227 (1997); *LTV Steel Co., Inc. v. Shalala (In re Chateaugay Corp.),* 53 F.3d 478, 491-93 (2d Cir.) (distinguishing "statutes burdening real and tangible property" from "those [as in the case at hand] requiring direct transfers of money to the government", and holding: Tucker Act does not "remove from the federal district courts jurisdiction over an action for declaratory relief where no money damages have been requested"; *Duke Power* demonstrates "the clear availability of declaratory relief for asserted Takings Clause violations"), *cert. denied,* 516 U.S. 913, 116 S.Ct. 298, 133 L.Ed.2d 204 (1995); *Southeast Kan. Comty. Action Program, Inc. v. Secretary of Agric.,* 967 F.2d

1452, 1456-57 (10th Cir.1992) (taking claim based on United States Department of Agriculture's failure to renew contract to administer federal child nutrition program; Tucker Act inapplicable when declaratory and injunctive relief sought).

More than a decade after *Monsanto* was decided, the Court in *Babbitt v. Youpee,* 519 U.S. 234, 242-43, 117 S.Ct. 727, 136 L.Ed.2d 696 (1997), affirmed declaratory and injunctive relief in an action challenging the constitutionality of a federal statute providing for escheat of fractional interests in land. Although at issue was whether there had been a taking, rather than the remedy that could be provided, *Babbitt* lends support to the conclusion that *Monsanto* and *Williamson County* do not categorically prohibit such relief for taking claims, especially where, as here, the claim is not against the United States (thus, Tucker Act not in play).

In 1998, the Court considered a taking claim by a company no longer involved in the coal industry, challenging the constitutionality of the Coal Industry Retiree Health Benefit Act of 1992, 26 U.S.C. §§ 9701-9722. *Eastern Enters. v. Apfel,* 524 U.S. 498, 118 S.Ct. 2131, 141 L.Ed.2d 451 (1998). A four-Justice plurality concluded that the Act violated the Takings Clause, and that the challenged provisions should be enjoined as applied to Eastern. *Id.* at 538, 118 S.Ct. 2131.

Citing *Monsanto,* the plurality acknowledged that "a claim [against the United States] for just compensation under the Takings Clause must be brought to the Court of Federal Claims in the first instance, unless Congress has withdrawn the Tucker Act grant of jurisdiction in the relevant statute". *Id.* at 520, 118 S.Ct. 2131. But, Eastern was not seeking compensation; instead, similar to the case at hand, it was requesting "a declaratory judgment that the Coal Act violates the Constitution and a corresponding injunction against the . . . enforcement of the Act as to Eastern". *Id.* "Such equitable

relief is arguably not within the jurisdiction of the Court of Federal Claims under the Tucker Act." *Id.*

The plurality noted the split among the Courts of Appeals regarding whether, for claims against the United States, equitable relief was available under the Takings Clause when just compensation had not been sought under the Tucker Act. *Id.* at 520-21, 118 S.Ct. 2131. Citing *Preseault* and *Monsanto,* the plurality acknowledged that the "Court's precedent can be read to support the . . . conclusion that regardless of the nature of relief sought, the availability of a Tucker Act remedy renders premature any takings claim in federal district court". *Id.* at 521, 118 S.Ct. 2131. But, because the Coal Act mandated payments to a privately-operated fund, monetary relief against the United States was not an available remedy. *Id.* The plurality reasoned: "Congress could not have contemplated that the Treasury would compensate coal operators for their liability under the Act, for '[e]very dollar paid pursuant to a statute would be presumed to generate a dollar of Tucker Act compensation'". *Id.* (quoting *Chateaugay,* 53 F.3d at 493). "Accordingly, the 'presumption of Tucker Act availability must be reversed where the challenged statute, rather than burdening real or physical property, requires a direct transfer of funds' mandated by the Government." *Id.* (quoting *Chateaugay,* 53 F.3d at 493). "In that situation, a claim for compensation 'would entail an utterly pointless set of activities.'" *Id.* (quoting *Riley,* 104 F.3d at 401).

The plurality stated *Duke Power* had "explained" that "the Declaratory Judgment Act allows individuals threatened with a taking to seek a declaration of the constitutionality of the disputed governmental action before potentially uncompensable damages are sustained". *Id.* (internal quotation marks and citation omitted). And, it noted that, in analogous situations, the Court had "assumed the lack of a compensatory remedy . . . for Takings Clause violations

without discussing the applicability of the Tucker Act". *Id.* at 521-22, 118 S.Ct. 2131 (citing *Babbitt,* 519 U.S. at 243-45, 117 S.Ct. 727; *Hodel v. Irving,* 481 U.S. 704, 716-18, 107 S.Ct. 2076, 95 L.Ed.2d 668 (1987)). The plurality noted also that, without addressing the basis of its jurisdiction, the Court had "upheld similar statutory schemes against Takings Clause challenges". *Id.* at 522, 118 S.Ct. 2131 (citing *Concrete Pipe & Prods. of Cal., Inc. v. Construction Laborers Pension Trust for Southern Cal.,* 508 U.S. 602, 641-47, 113 S.Ct. 2264, 124 L.Ed.2d 539 (1993); *Connolly v. Pension Benefit Guar. Corp.,* 475 U.S. 211, 221-28, 106 S.Ct. 1018, 89 L.Ed.2d 166 (1986)). Finally, the plurality stated that, although it was "'not bound by previous exercises of jurisdiction in cases in which [the Court's]power to act was not questioned but was passed *sub silentio,* neither should [it] disregard the implications of an exercise of judicial authority assumed to be proper' in previous cases". *Id.* (quoting *Brown Shoe Co. v. United States,* 370 U.S. 294, 307, 82 S.Ct. 1502, 8 L.Ed.2d 510 (1962)).

Therefore, based on the nature of the alleged taking, which required Eastern to make payments to a privately operated fund for retirement benefits for former coal industry workers, the plurality concluded: "the declaratory judgment and injunction sought by [Eastern] constitute an appropriate remedy under the circumstances, and . . . it is within the district courts' power to award such equitable relief". *Id.*

Needless to say, the challenged governmental action in the case at hand does not merely burden real or personal property; instead, it involves TEAJF's taking all of the interest earned on client-funds in IOLTA accounts. In that sense, it is more analogous to the challenged governmental actions in *Eastern Enterprises, Chateaugay,* and *Riley,* which involved payment of money to, or to support, a government program, than to the challenged governmental actions in *Monsanto* and *Williamson County,* which burdened real or

personal property, and in which a procedure for seeking just compensation was available. Again, as *Chateaugay* explained, "where the challenged statute requires a person or entity to pay money to the government, it must be presumed that [the government] had no intention of providing compensation for the deprivation". *Chateaugay,* 53 F.3d at 493. "For such cases, use of the [just compensation] remedy would entail an utterly pointless set of activities, as '[e]very dollar paid pursuant to a statute would be presumed to generate a dollar of [just] compensation'". *Riley,* 104 F.3d at 401 (quoting *Chateaugay,* 53 F.3d at 493).

Restated, because the purpose of IOLTA is to take the interest generated from client-funds and use it to fund legal services for the indigent, it is obvious that the program makes no provision for payment of just compensation. If the interest earned on client-funds were available as just compensation for the clients, the very purpose of the program would be thwarted; therefore, it would defy logic, to say the least, to presume the availability of a just compensation remedy. Because there is no "reasonable, certain and adequate provision for obtaining compensation . . . at the time of the taking", *Williamson County,* 473 U.S. at 194, 105 S.Ct. 3108, the ripeness doctrine does not preclude declaratory or injunctive relief.[12]

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[12] The dissent asserts at 200 that, by addressing ripeness, we have "buil[t]a straw man [and] then take[n] great pains to knock the stuffing out of him", because Appellees "have made no such argument in this appeal". But, as the dissent acknowledges, *id.*, Appellees do contend Appellants cannot claim injunctive relief because they have not availed themselves of available state remedies, citing, *inter alia, Williamson County*. The state remedies referenced by the dissent and Appellees are not "available". As the dissent acknowledges at 203, the Texas IOLTA program's provision for refunds is available only for a "client whose funds are wrongly placed in IOLTA accounts".

(continued...)

2.

Consistent with the conclusion by the district court, the Justices of the Texas Supreme Court claim they are legislatively immune from suit for injunctive relief. The district court's ruling was premised on its conclusion that the Justices do not possess the power to enforce compliance with the IOLTA program. *Washington Legal Found.*, 86 F.Supp.2d at 624.

a.

As discussed, the Justices, together with the other Appellees, conceded on the prior appeal to our court that they are subject to Appellants' prospective injunction claims. *Washington Legal Found.*, 94 F.3d at 1005. As also discussed, that concession is binding on them.

b.

In the alternative, and for the reasons that follow, we hold that, because the Texas Supreme Court has the power to suspend attorneys who do not comply with IOLTA rules, the Justices are not entitled to legislative immunity from this action.

Pursuant to its inherent power to regulate the practice of law in Texas, the Texas Supreme Court created the IOLTA program and its underlying rules. TEXAS RULES OF COURT--STATE, Rules Governing the State Bar of Texas Art. XI, § 2(D). Rule 24 addresses compliance with the IOLTA program: a Texas attorney is required to annually

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(footnote continued)

Nor, contrary to the dissent, do we rely on the ripeness doctrine to conclude that the claim for equitable relief is substantively viable. *Dissent* at 200. Instead, we hold the claim is substantively viable because there has been an unconstitutional taking of private property, and there is no mechanism for payment of just compensation.

provide a written statement of compliance to TEAJF; if he fails to do so, TEAJF contacts him and attempts administratively to resolve the non-compliance; if unsuccessful, TEAJF places his name on a list of non-compliant attorneys and sends him a notice; if, within 30 days, the non-compliant attorney still refuses to file the required compliance statement, the State Bar of Texas notifies the Clerk of the Texas Supreme Court of such non-compliance; and the attorney "shall be" immediately suspended by the Clerk from the practice of law until the compliance statement is filed. *See* TEAJF rule 24; *Washington Legal Found.*, 86 F.Supp.2d at 622.

Applicable here is the holding in *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719, 725-26, 100 S.Ct. 1967, 64 L.Ed.2d 641 (1980). There, a consumer organization brought an action against the Virginia Supreme Court and its chief justice for a declaration they had violated the First and Fourteenth Amendments by promulgating and enforcing rules prohibiting attorney advertising. The Supreme Court held the court and its chief justice, although legislatively immune from claims regarding the adoption of the challenged rules, were properly held liable in their enforcement capacities. *Id.* at 736, 100 S.Ct. 1967.

III.

For the foregoing reasons, we REVERSE and REMAND this case to the district court for entry, consistent with this opinion, of declaratory and injunctive relief.

REVERSED and REMANDED.

WIENER, Circuit Judge, dissenting:

In *Phillips v. Washington Legal Foundation*[13] the Supreme Court held that the plaintiffs in the instant case had a property right in the interest income from their funds deposited in IOLTA accounts. In dissent, Justice Souter criticized the majority's decision to determine that a property right existed in isolation from the questions (1) whether a "taking" had occurred, and (2) if so, what compensation, if any, might be owed. Justice Souter wrote that "if it should turn out that the 'just compensation' for any taking was zero, then there would be no practical consequence for purposes of the Fifth Amendment in recognizing a client's property right in the interest in the first place; any such recognition would be an inconsequential abstraction."[14]

After a full trial on remand, the plaintiffs in this case ("IOLTA II") have brought us to precisely the moment Justice Souter foretold by proving that their loss – and, therefore, the "just compensation" that they are due – is zero. By its literal terms, the Fifth Amendment can be violated only by governmental failure to pay just compensation: "The Fifth Amendment does not proscribe the taking of property; it proscribes taking without just compensation."[15] This

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[13] 524 U.S. 156, 118 S.Ct. 1925, 141 L.Ed.2d 174 (1998).

[14] *Phillips,* 524 U.S. at 174-75, 118 S.Ct. 1925 (Souter, J., dissenting). Souter also compares the holding of *Hooker v. Burr,* 194 U.S. 415, 419, 24 S.Ct. 706, 48 L.Ed. 1046 (1904) ("If a contractual obligation is impaired, but the obligor is 'not injured to the extent of a penny thereby, his abstract rights are unimportant.' ").

[15] *Williamson County Regional Planning Comm'n v. Hamilton Bank of Johnson City,* 473 U.S. 172, 194, 105 S.Ct. 3108, 87 L.Ed.2d 126 (1985); *see also Suitum v. Tahoe Reg'l Planning Agency,* 520 U.S. 725, 734, 117 S.Ct. 1659, 137 L.Ed.2d 980 (1997) (noting that "only takings without 'just compensation' infringe th[e Fifth] Amendment"); *First English Evangelical Lutheran Church of Glendale v. Los Angeles County, Cal.,* 482 U.S. 304, 315, 107 S.Ct. 2378, 96 L.Ed.2d 250 (1987) (stating that the Fifth Amendment "is designed not to limit the governmental

(continued...)

constitutional truism convinces me that even if the Texas IOLTA program should involve the government's "taking" of "property," it would not violate the plaintiffs' constitutional rights because just compensation for zero is zero. I therefore respectfully dissent.

I.

At the outset, I must take issue with the majority's assertion that the defendants-appellees[16] have conceded that the plaintiffs-appellants[17] are entitled to equitable relief: The defendants have done no such thing. In our previous decision in this case ("*IOLTA I*"), we stated – as a parting-shot discussion of Eleventh Amendment immunity – that "the defendants concede that they are *subject to* the plaintiffs' prospective injunction *claims.*"[18] We then concluded that the defendants were immune from a claim for

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(footnote continued)

interference with property rights *per se,* but rather to secure *compensation* in the event of otherwise proper interference amounting to a taking").

[16] The Texas Equal Access to Justice Foundation, its chairman, and the Texas Supreme Court justices.

[17] The Washington Legal Foundation, attorney Michael J. Mazzone, and client William R. Summers.

[18] *Washington Legal Found. v. Texas Equal Access to Justice Found. (IOLTA I),* 94 F.3d 996, 1005 (5th Cir.1996) (emphasis added). In context, the entire paragraph reads thus: Finally, the district court also granted the defendants' request for immunity under the Eleventh Amendment with respect to the plaintiffs' claim for monetary restitution. The parties now only dispute whether the district court erred by declaring the defendants immune to the plaintiffs' restitution claim. The parties do not seriously challenge this portion of the district court's ruling; the defendants concede that they are subject to the plaintiffs' prospective injunction claims and the plaintiffs admit that their "principal concern all along has been in obtaining prospective injunctive relief." We suggest another reason for the parties' lackadaisical approach to this part of the decision: they realize that the district court is correct. *Id.*

monetary restitution.[19] There is a vast difference between conceding that the Eleventh Amendment is not a *bar* to the assertion of a *claim,* on the one hand, and conceding *entitlement* to the *relief sought* by asserting a claim, on the other.

I am sure that, as it states, the panel majority understands the distinction between a party being "subject to" a claim and the party opposite being "entitled to" equitable relief.[20] Yet, despite this voiced cognizance, the majority still concludes that the appellees somehow take a position here that is inconsistent with their former concession by arguing on appeal that equitable relief is unavailable. In doing so, the majority strains Judge Wisdom's simple jurisdictional statement in IOLTA I to the point of incredulity. Consistent with a jurisdictional submission, appellees may still vigorously refute the availability of equitable relief for appellants on grounds unrelated to jurisdiction. The appellees in their brief to this court in IOLTA II argue that equitable relief is not available to the appellants because (1) the appellants have failed to seek state administrative remedies and (2) compensation, not injunctive relief, is the only proper remedy for a 5th Amendment violation. Neither of these contentions undermine a concession that appellees are subject to, *i.e.*, must address, the appellants' claims for injunctive relief.

Moreover, the majority's willingness to dispose of the issue based on its reading of the admission is premature. Even assuming, *arguendo,* that appellees have taken an inconsistent position by reasserting an 11th Amendment claim on appeal, the inquiry cannot possibly end there. At most, under the majority's reading, the appellees would have

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[19] *Id.*

[20] The majority at 190, n. 11.

been holding an inconsistent position on the necessity to deal with the appellants' claims. Determining the apparent inconsistency, for argument's sake, against the appellees only clears the initial jurisdictional hurdle; it does not, in any way, resolve the merits of the remedy issue. Yet, the majority decides both jurisdiction and the merits based on the concession, and, indeed, only resumes discussion of the merits of the prospective injunction claim "in the alternative." Hence, despite the majority's protestations to the contrary, it has effectively equated appellees' concession to hear and respond to appellants' remedy claims with a concession that appellees will not or even cannot contest those claims.

What the defendants-appellees actually wrote in their IOLTA I appellate brief is this: "Appellees concede that the Eleventh Amendment is not a jurisdictional bar to the claims asserted by Appellants for prospective injunctive relief against Appellee Newton[21] as a state official." At another point in their brief, the defendants wrote:

> The Texas IOLTA Program Appellees concede that the Eleventh Amendment is *not a jurisdictional bar* to Appellants' claims. Rather, the Texas IOLTA Program Appellees contend *that they are entitled to Eleventh Amendment immunity from* Appellants' claims for damages, including restitution, and *any other claim than a claim for prospective injunctive relief.*[22]

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[21] Defendant W. Frank Newton, then-chairman of the Texas Equal Access to Justice Foundation.

[22] Emphasis added. Similarly, defendants-appellees the Texas Supreme Court justices wrote in their 1995 brief to this court in *IOLTA I*: "*Even assuming that some violation of the Constitution could be established,* (continued...)

Thus, the defendants successfully asserted Eleventh Amendment immunity from monetary damages while acknowledging nothing more than that the Eleventh Amendment does not bar governmental defendants from having to defend claims of prospective relief on the merits.

This is no quibble on my part: A concession that something is *not a bar* to a *claim* is a far cry from a concession that a plaintiff is *entitled* to *relief.* As the defendants have vigorously contested the plaintiffs' claims both times that they have come before this court, I must protest the majority's attempts to portray the defendants as having conceded the issue of the plaintiffs' entitlement to equitable relief.

II.

The Takings Clause of the Fifth Amendment reads, in pertinent part: "nor shall private property be taken for public use, without just compensation."[23] To prove a violation of the Takings Clause, a plaintiff must prove that (1) property (2) has been taken for public use (3) without just compensation.

The Supreme Court held in *Phillips* that the plaintiffs have a property right in the interest income on their IOLTA accounts, satisfying part one of the three-part inquiry. And I am willing to concede for purposes of this dissent (even though I would have resolved the issues differently) that a

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(footnote continued)

however, the relief available to plaintiffs is limited to prospective injunctive relief only." (emphasis added). I will not address the justices' claim of legislative immunity because I discern no constitutional violation.

[23] U.S. Const. amend. V.

"taking" occurred in this case, satisfying part two.[24] Although this puts the plaintiffs two-thirds of the way home, that is as far as they get – legitimately, at least. Because the Fifth Amendment does not forbid the government from (1) taking (2) property, but requires only that, when property is taken, "just compensation" be paid, "the crux of this case rests on the issue of just compensation."[25] And, clearly, "just compensation" is payment of value for equal value.[26] None can argue that the equal value of zero is anything other than zero – at least not forthrightly.

The majority discourses on the nature of takings remedies in the abstract, but chooses to ignore the specific factual findings made by the district court in its detailed opinion in this case. That court conducted a two-day bench trial, during which it considered evidence that the plaintiffs presented regarding three separate accounting approaches to handling client funds – in-firm pooling, sub-accounting,[27] and the net benefit theory. Weighing all the evidence presented, the court concluded that the only plaintiff with funds in a Texas IOLTA account, William R. Summers, suffered no loss – zero. Indeed, Mr. Summers himself testified candidly and unequivocally to that fact.

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[24] As the majority points out, there is no dispute that any taking in this case was "for public use."

[25] *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 86 F.Supp.2d 624, 637 (W.D.Tex.2000).

[26] *See United States v. Reynolds*, 397 U.S. 14, 16, 90 S.Ct. 803, 25 L.Ed.2d 12 (1970).

[27] Sub-accounting is a banking product that allows a law firm to open a master account and link a sub-account for each client. Although apparently not now available in Texas, a firm theoretically could open a sub-account using an out-of-state bank.

Solidly grounded in trial testimony, the court found that the plaintiffs proved no loss under any of the three accounting approaches that they proffered: (1) Mr. Summers's funds could not earn net interest if placed in a non-IOLTA pooled account with funds of a law firm's other clients; (2) the plaintiffs did not establish that their funds could earn net interest in a sub-account, given the costs associated with such accounts; and (3) the plaintiffs failed to prove that they could gain a "net benefit" from their funds even if they could not earn net interest on them. The court concluded soundly that the plaintiffs did not satisfy their burden of proof:

> Plaintiffs failed to establish an actual number denominating Mr. Summers' loss. With regard to *this case* and *Mr. Summers'* monies, Plaintiffs have failed to carry their burden of proof. Although this case turns on endless abstractions and near impossible mathematical conclusions it is without doubt that at a minimum Plaintiffs must present evidence to this Court that Mr. Summers is materially worse off because of IOLTA. At trial Mr. Summers testified that he is no worse off because of IOLTA.[28]

The plaintiffs insist that the district court's factual conclusions contain errors, most notably the court's failure to acknowledge that the rules determining whether client funds are to be placed into IOLTA accounts require attorneys to

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[28] *Washington Legal Found.*, 86 F.Supp.2d at 643; *see also Marion & Rye Valley Ry. Co. v. United States*, 270 U.S. 280, 282, 46 S.Ct. 253, 70 L.Ed. 585 (1926) (affirming denial of a compensation claim and stating that even if a taking technically occurred, "[n]othing was recoverable as just compensation, because nothing of value was taken from the company, and it was not subjected by the government to pecuniary loss").

consider the administrative costs of opening and maintaining non-IOLTA accounts, but not IOLTA accounts.[29] When these costs are factored in, argue the plaintiffs, clients could realize a *net benefit, i.e.*, a smaller gap between interest earned and the lawyers' costs (ultimately passed along to the clients) of maintaining the account even though clients can never realize *net interest.*

The plaintiffs are just plain wrong. The record confirms that the district court specifically considered evidence on this issue and rejected the claim.[30] The court's conclusion jibes with its finding that the costs of administering the money placed in a non-IOLTA account exceed those in an IOLTA account.[31] The plaintiffs' other allegations of factual error are equally feckless.

At no point do the plaintiffs ground their theoretical arguments in an assertion of any specific monetary loss suffered by Mr. Summers – indeed, they could not. This failure absolutely precludes their ability to demonstrate clear

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[29] Texas attorneys may place client funds in IOLTA accounts only if:

> such funds, could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the account, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain the interest on such funds for the client.

Tex.R. Equal Access Rule 6.

[30] *Washington Legal Found.*, 86 F.Supp.2d at 638 ("Plaintiffs argue that client funds can generate a net benefit to the client when not placed in IOLTA. The Court finds that the testimony at trial established otherwise. There are innate costs to the firm or lawyer in a non-IOLTA account that differ from those in an IOLTA account.").

[31] *Id.* at 646. The defendants attribute this fact to lower in- firm administrative costs for IOLTA accounts and the fact that bank fees on those accounts typically are paid by IOLTA or waived by banks.

error in the district court's factual finding that Mr. Summers's loss was "zero."[32] The Supreme Court defines "just compensation" for a taking as "the full monetary equivalent of the property taken."[33] Payment of just compensation is an effort to put the claimant, from his own viewpoint, "'in as good a position pecuniarily as if his property had not been taken.'"[34] It follows inescapably that when the owner's loss is zero, he is owed no compensation.[35]

Unable to prove any monetary loss whatsoever, the plaintiffs have abandoned their claim for monetary restitution.[36] Instead they seek only declaratory and

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[32] *Id.* at 643. The court's factual findings and inferences are reviewed for clear error. Fed.R.Civ.P. 52(a); *Anderson v. City of Bessemer City,* 470 U.S. 564, 574, 105 S.Ct. 1504, 84 L.Ed.2d 518 (1985); *Robicheaux v. Radcliff Material, Inc.,* 697 F.2d 662, 666 (5th Cir.1983).

[33] *Reynolds,* 397 U.S. at 16, 90 S.Ct. 803; *see also Kimball Laundry Co. v. United States,* 338 U.S. 1, 5, 69 S.Ct. 1434, 93 L.Ed. 1765 (1949) (disregarding subjective value as a measure of compensation: "In view, however, of the liability of all property to condemnation for the common good, loss to the owner of nontransferable values deriving from his unique need for property or idiosyncratic attachment to it, like loss due to an exercise of the police power is properly treated as part of the burden of common citizenship.").

[34] *United States v. 564.54 Acres Land,* 441 U.S. 506, 510, 99 S.Ct. 1854, 60 L.Ed.2d 435 (1979) (quoting *Olson v. United States,* 292 U.S. 246, 255, 54 S.Ct. 704, 78 L.Ed. 1236 (1934)); *see also Boston Chamber of Commerce v. City of Boston,* 217 U.S. 189, 195, 30 S.Ct. 459, 54 L.Ed. 725 (1910).

[35] The finding of zero compensation due distinguishes this case from a similar challenge currently on en banc rehearing by the Ninth Circuit. The Ninth Circuit panel opinion, now vacated, would have remanded that case to the trial court to determine what compensation was owed. *Washington Legal Found. v. Legal Found. of Washington,* 236 F.3d 1097, *vacated,* 248 F.3d 1201 (9th Cir.2001).

[36] We have held that the Eleventh Amendment bars the plaintiffs' monetary reimbursement claim. *IOLTA I,* 94 F.3d at 1005.

injunctive relief against the Texas IOLTA program. Yet these equitable remedies, standing alone, are obviously inappropriate to the situation at hand, in which the absence of economic loss and the concomitant absence of compensation due proves that there has been no Fifth Amendment violation at all.

We need not pause to ponder whether freestanding equitable relief can *ever* be an appropriate remedy for an unconstitutional taking, for *in this case* there is no unconstitutional (*i.e.*, uncompensated) taking. This immutable fact eschews any justification for legal or equitable remedy whatsoever. The plaintiffs are absolutely wrong to argue – and the panel majority to accept – that their "entitlement to just compensation is of limited relevance to this appeal." To the contrary, such entitlement – or the absence thereof – lies at the very heart of this appeal. As the plaintiffs have not been denied just compensation, they could not prove – and have not proved – any violation of their constitutional rights.

III.

The panel majority nevertheless strains to justify its award of prospective equitable remedies here by implying that the *ripeness* doctrine – of all things – does not preclude them. But not precluding a remedy is far different from justifying a remedy. On its path to injunctive relief, the majority first builds a straw man then takes great pains to knock the stuffing out of him, based on the defendants' apparent argument at an earlier stage of this case that the plaintiffs should have sued for compensation in state court. The defendants have made no such argument in this appeal, IOLTA II, a fact that the plaintiffs themselves now call to our attention. Rather, the defendants address ripeness only to make the valid point that plaintiff Summers has failed to seek and exhaust the available administrative remedy of a refund of any interest due to him under the IOLTA rules. The

district court did not reach this issue, and I am willing to concede it for the purposes of this dissent, accepting the plaintiffs' assertions that they were unaware of the refund policy until 1998 and that a state suit would be futile. The outcome of this case does not turn, however, on any issue of ripeness.[37] The mere fact that this claim may be ripe does not mean that it is substantively viable, and it certainly does not justify the award of equitable remedies here.

The cases relied on by the majority to address the (nonexistent) ripeness issue are easily distinguishable. *Eastern Enterprises v. Apfel*,[38] *LTV Steel Co. v. Shalala (In re Chateaugay Corp.)*,[39] and *Student Loan Marketing Association v. Riley*[40] all analyze the threshold jurisdictional question of whether a federal court has the power to award equitable relief for a taking that involves a direct transfer of a determinable sum of money to the federal government, relieving the plaintiffs of the need first to sue for compensation in the Court of Federal Claims under the Tucker Act.[41] In each of these three cases, which involve

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[37] *See Texas v. United States*, 523 U.S. 296, 300, 118 S.Ct. 1257, 140 L.Ed.2d 406 (1998) ("A claim is not ripe for adjudication if it rests upon contingent future events that may not occur as anticipated, or indeed may not occur at all.") (internal quotations omitted).

[38] 524 U.S. 498, 118 S.Ct. 2131, 141 L.Ed.2d 451 (1998).

[39] 53 F.3d 478, 492 (2d Cir. 1995) (rejecting claim that Coal Act resulted in unconstitutional taking after noting that "the question of jurisdiction in the case masks a broader question of ripeness: Can a takings claim ever be brought in a district court without first seeking compensation in the Court of Federal Claims?").

[40] 104 F.3d 397 (D.C.Cir.1997) (rejecting claim that 0.3 percent "offset fee" on principal amount of each student loan held by the Student Loan Marketing Association ("Sallie Mae") imposed an unconstitutional taking).

[41] 28 U.S.C. § 1491.

alleged regulatory takings with a quantifiable economic impact on the plaintiffs, the court found that a suit for money damages would be pointless because the claimed (in two of the three cases, failed claim of a) taking would have necessitated a dollar-for-dollar monetary reimbursement. Unlike the instant case, these cases did not involve plaintiffs whose monetary compensation claim was pointless because they had gone to trial and lost, having suffered no monetary loss. The Declaratory Judgment Act may offer one remedy for an unconstitutional taking, that is, an uncompensated taking; it is no substitute, however, for proof of loss.[42]

Another case relied on by the majority, *Southeast Kansas Community Action Program Inc. v. Secretary of Agriculture,*[43] implicated a due process claim – *not a takings case at all* – in which the plaintiffs' primary purpose in bringing suit was to receive the classic due process remedy: a hearing. Finally, in *Babbitt v. Youpee,*[44] the Court approbated equitable relief in a situation in which the statute in question already had been found to take interests in other lands valued at $100, $1,816, and $2,700, with no possibility of compensation.[45] In *Youpee,* those taken property interests

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[42] I note further that two of these three cases apply the ad hoc takings analysis of *Penn Central Transportation Co. v. City of New York,* 438 U.S. 104, 124, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978), and *Kaiser Aetna v. United States,* 444 U.S. 164, 175, 100 S.Ct. 383, 62 L.Ed.2d 332 (1979), which the majority rejects in favor of a *per se* analysis. *See Eastern Enters.,* 524 U.S. at 523-24, 118 S.Ct. 2131; *Chateaugay,* 53 F.3d at 494. The third case found that a regulatory action was not a taking at all because the burden was "'a fair approximation of the costs of benefits supplied.'" *Riley,* 104 F.3d at 402 (quoting *United States v. Sperry Corp.,* 493 U.S. 52, 60, 110 S.Ct. 387, 107 L.Ed.2d 290 (1989)).

[43] 967 F.2d 1452 (10th Cir.1992).

[44] 519 U.S. 234, 117 S.Ct. 727, 136 L.Ed.2d 696 (1997).

[45] *Hodel v. Irving,* 481 U.S. 704, 107 S.Ct. 2076, 95 L.Ed.2d 668 (1987).

were worth $1,239 – not "zero." Once the Supreme Court determined that an amendment to the statute aimed at curing that defect still did not rectify the uncompensated taking, it sanctioned equitable relief against enforcement of the statute, just as it had upheld the award of appropriate relief before the unconstitutional provision was amended. In affirming the Ninth Circuit, the Supreme Court quoted that circuit court's suggestion that, although the government could not constitutionally apply the statutory scheme, it could obtain the interests by other means, such as purchasing the land in question or condemning it and paying just compensation to the plaintiffs.[46]

The panel majority seeks to rely on these cases by analogy to justify an award of equitable relief alone, but they simply are not analogs to this case. The reasoning in that line of cases cannot be stretched far enough to cover the facts at hand; yet the plaintiffs, having themselves proved that they have not been denied just compensation, nonetheless ask us to impose a prior restraint on a program that has found favor in all fifty states.[47] That the plaintiffs – and others – may (and obviously do) oppose on ideological grounds a state program funded with IOLTA interest does not vest us with the judicial right to meddle with that plan, which itself does not violate the U.S. Constitution.[48]

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[46] *Youpee,* 519 U.S. at 242, 117 S.Ct. 727 (citing *Youpee v. Babbitt,* 67 F.3d 194, 200 (9th Cir.1995)). *Irving* and *Youpee* involved attempts to reduce highly fractionated interests in Indian-owned lands.

[47] Every state, plus the District of Columbia and the Virgin Islands, operates an IOLTA program.

[48] *See* Donald L. Beschle, *The Supreme Court's IOLTA Decision: Of Dogs, Mangers, and the Ghost of Mrs. Frothingham,* 30 Seton Hall L.Rev. 846, 867 (2000) ("In *Phillips,* what is being 'taken' is the right to exclude in its purest form – that is, the psychological satisfaction of denying a benefit to another. This is the legal equivalent of the legendary

(continued...)

And make no mistake about it: We are not here contemplating some threatened taking that the mandatory Texas IOLTA program, which became effective in 1989, might inflict on some as-yet unidentified plaintiff, or on these specific plaintiffs at some future date. This case is about these plaintiffs, here and now. Funds owned by Mr. Summers – a $1000 retainer Mr. Summers paid to Mr. Mazzone in 1993, and a $250 retainer he paid in 1999 – have been held in IOLTA accounts since 1993, prior to the commencement of this litigation and throughout its pendency as well. The plaintiffs now have had a full trial, during which they failed to carry their burden of proving that they are due any just compensation whatsoever. They have not shown clear error in the district court's conclusion that they are due no compensation at all, or a legal basis for awarding prospective relief. And because it cannot, the panel majority has not identified any specific amount that the plaintiffs have not been compensated; neither has the majority demonstrated any valid support for decreeing injunctive or declaratory relief under these facts. To me, it is just that plain.

IV.

To recap, the Takings Clause "was not meant to prevent the government from pursuing legitimate goals; it was meant only to assure that no individual would be unduly burdened in the process of doing so."[49] The Texas IOLTA program, which generates approximately $5 million a year in total revenues from attorney trust funds – nominal and short-term deposits from individual clients as well as monies

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(footnote continued)

'dog in the manger,' a metaphor in which a dog aggressively prevents other animals from access to something – hay in the manger – that is of no practical use to the dog itself.").

[49] *Id.* at 892.

from for-profit corporations and partnerships – does not implicate the classic takings problem of fairness, in which an individual or small group is singled out to bear burdens that should be borne by the public as a whole.[50] Neither does it offend the original purpose of the Takings Clause, which was narrowly crafted to require compensation only for physical takings of tangible property by the federal government.[51] The clause was never intended to usurp the role of the people in deciding what social programs are appropriate, and "has not been understood to be a substantive or absolute limit on the government's power to act. The Clause operates as a conditional limitation, permitting the government to do what it wants so long as it pays the charge."[52]

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[50] *See Penn Central,* 438 U.S. at 123-24, 98 S.Ct. 2646. The plaintiffs argue that "virtually all client funds" held by attorneys end up in IOLTA accounts, spreading the "burden" of funding legal services for the poor among many users of the court system, not a small group.

[51] *See, e.g.,* William Michael Treanor, *The Original Understanding of the Takings Clause and the Political Process,* 95 Columbia L.Rev. 782, 859-60 (1995) ("[T]he federal Takings Clause and its predecessor clauses, as they were originally understood, divided governmental actions affecting property into two groups. When the government physically took property, it owed compensation. Any other governmental action, no matter how severely it affected the value of property, did not give rise to a compensation requirement. This requirement applied to physical takings because the framers believed that majoritarian decisionmaking processes would not give fair consideration to the individual's interest in not having her property physically seized by the government."

"The clause sought to remedy failures in the political process. But the underlying idea was *not* that all majoritarian decisions should be reviewed to determine whether the process behind any particular decision was fair or unfair. Rather, heightened constitutional protection was provided only for the limited category of decisions in which unfairness was most likely.").

[52] *See Eastern Enters.,* 524 U.S. at 545, 118 S.Ct. 2131 (Kennedy, J., concurring in the judgment and dissenting in part).

It is important to remember that we cannot substitute concerns about due process – addressing the legitimacy and purpose of Texas's operation of its IOLTA program, which I perceive to be the plaintiffs' real complaint in this case – for concern about a taking, which turns on the availability of just compensation.[53] Our role is strictly limited to ensuring that initiatives such as the Texas IOLTA program provide a mechanism for providing "just compensation" for any taken property.[54] The Texas IOLTA program has just such a mechanism, a provision for refunding any interest that could have been earned by a client whose funds are wrongly placed in IOLTA accounts. And, the state routinely grants requests for such refunds.

The plaintiffs in this case have had their day in court, and have themselves proved that they have not been denied "just compensation" for any purported governmental taking of property that they may have experienced from the enforcement of the Texas IOLTA program. No deprivation of just compensation means no possibility of a constitutional violation. As I would in all respects affirm the judgment of the district court, I respectfully dissent.[55]

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[53] *See id.*

[54] *See Williamson County,* 473 U.S. at 194, 105 S.Ct. 3108 (explaining that the Fifth Amendment requires the government to "provide [ ]an adequate process for obtaining compensation").

[55] Because the majority did not address the plaintiff's claimed First Amendment violation, I do not, either. I merely note in passing that the argument will fall of its own weight.

UNITED STATES DISTRICT COURT, W.D. TEXAS,
AUSTIN DIVISION

No. A-94-CA-081 JN.

WASHINGTON LEGAL FOUNDATION, et al.,

v.

TEXAS EQUAL ACCESS TO JUSTICE
FOUNDATION, et al.

January 28, 2000

MEMORANDUM OPINION AND ORDER

NOWLIN, District Judge.

Before the Court is the above-entitled cause of action. A bench trial was held before this Court on September 22, 1999 and September 23, 1999. Plaintiffs submitted Plaintiffs' Post-Trial Brief (Clerk's Doc. No. 141) on November 2, 1999. Defendants submitted Defendants' Post-Trial Brief (Clerk's Doc. No. 143) on November 29, 1999. Having considered the testimony and evidence presented at trial, as well as the relevant law, the Court enters the following Opinion and Order. This Memorandum Opinion and Order constitutes the Court's findings of fact and conclusions of law. *See* Fed.R.Civ.P. 52(a).

*I. Procedural Background*

The Plaintiffs in this cause of action are: the Washington Legal Foundation, a non-profit public interest law and policy center; Michael Mazzone, a Texas resident

and attorney licensed to practice law by the State Bar of Texas; and William Summers, a Texas resident and consumer of legal services. Plaintiffs bring this case pursuant to 42 U.S.C. § 1983 asserting that Defendants' mandatory Interest on Lawyers' Trust Account ("IOLTA") program violates the First and Fifth Amendments of the United States Constitution. The IOLTA program is implemented and overseen by Defendant the Texas Equal Access to Justice Foundation ("TEAJF"). In 1984, the Texas Supreme Court Justices adopted Article XI of the Rules of the State Bar of Texas which established the IOLTA program. In 1988, the Justices made the program mandatory. This Court entered an order on January 4, 2000 dismissing the Texas Supreme Court Justices on the basis of legislative immunity.

By Order dated January 19, 1995, this district court granted summary judgment for Defendants on the basis that Plaintiffs could not establish a constitutionally cognizable property interest because, but for the IOLTA program, no interest could be earned on the funds in the IOLTA account. *Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 873 F.Supp. 1, 7 (W.D.Tex.1995). The Fifth Circuit reversed this court, concluding that the interest earned on client funds held in IOLTA accounts is a property interest within the reach of the Fifth Amendment. *Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 94 F.3d 996 (5th Cir.1996). The Supreme Court affirmed the Fifth Circuit's decision and determined that the interest income generated by the Texas IOLTA program is the "private property" of the owner of the principal. *Phillips v. Washington Legal Foundation,* 524 U.S. 156, 118 S.Ct. 1925, 1934, 141 L.Ed.2d 174 (1998). This holding was limited to its determination of the existence of a property interest in the interest income. *Id.* The Supreme Court remanded the case for consideration of whether or not IOLTA funds have been "taken" by the State,

as well as the amount, if any, of just compensation due Plaintiffs. *Id.* Thus this Court must once again consider the fate of IOLTA.

*II. What is IOLTA?*

The Texas Interest on Lawyers Trust Account ("IOLTA") is fashioned from a complex web of federal banking regulations, state law, Internal Revenue Service Rulings, and ethical rules. All these rules work in conjunction to create a unique class of revenue which the state then directs to the delivery of legal services to low income individuals.

In 1980 Congress passed legislation creating Negotiable Order of Withdrawal ("NOW") accounts, which allowed federally insured banks to pay interest on demand accounts. 12 U.S.C. § 1832. Absent an agreement with the client, Texas ethical rules require lawyers to keep client funds separate from the attorney's funds and that these funds be available to the client upon demand. Tex. Disciplinary R. Prof. Conduct 1.14, *reprinted in* Tex. Gov't Code Ann., tit 2, subtit. G app. A (Vernon's Supp.1998) (Tex. State Bar R. Art. X, § 9). Before the creation of NOW accounts, lawyer trust accounts were almost without exception non-interest bearing accounts. Therefore, only banks benefitted from the deposits lawyers made into client trust accounts.

NOW accounts are permitted only for deposits that consist of funds "only where the entire beneficial interest is held by one or more individuals or by an organization which is operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes and which is not operated for profit." 12 U.S.C. § 1832(a)(2). For-profit corporations and partnerships are prohibited from earning interest on demand accounts. *Id.* The Federal Reserve Board, however, has interpreted § 1832(a) to convey that corporate funds may be held in NOW accounts if the funds are held in trust pursuant to a program in which charitable organizations

have the exclusive right to the interest earned. *See Phillips* at 159, 118 S.Ct. 1925 (citing Letter from Federal Reserve Board General Counsel Michael Bradfield to Donald Middlebrooks (Oct. 15, 1981)).

Article XI of the State Bar Rules of Texas provides that an attorney who receives funds that are "nominal in amount or are reasonably anticipated held for a short period of time" must place these funds in a separate interest- bearing NOW account that is denominated an IOLTA account. TEX. STATE BAR R., Art. XI, § 5(A); Tx. R. Equal Access Rule 4, 7 (West 1999). Under the IOLTA rules, an attorney must initially determine whether the funds are capable of earning a net interest for the client. *Id.* Rule 6. In making this determination the attorney must decide if:

> such funds, considered without regard to funds of other clients which may be held by the attorney, law firm, or professional corporation, could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the account, service charges, accounting costs, and tax reporting costs which would be incurred in attempting to obtain the interest on such funds for the client.

*Id.*

The Internal Revenue Service does not attribute income earned in an IOLTA account to the individual client for federal income tax purposes so long as the client has no control over the decision whether to place the funds in the IOLTA account and does not designate who will receive the interest generated by the account. *See* Rev.Rul. 81-209, 1981-2, C.B. 16; Rev.Rul. 87-2, 1987-1 C.B. 18. Under the Internal Revenue Code any interest from a non-IOLTA

pooled account or sub-account must be reported separately. Rev.Rul. 87-2, 1987-1 C.B. 18.

The TEAJF is the designated beneficiary for the interest earned on the funds in the Texas IOLTA Program. The TEAJF is a non-profit organization established by the Supreme Court of Texas. TEX. STATE BAR. R., Art. XI, §§ 3, 4; Tx. R. Equal Access Rule 9(a). The TEAJF distributes these funds to nonprofit organizations whose primary purpose is the delivery of legal services to low income individuals. Tx.R. Equal Access Rule 10.

The parties to this litigation agree that the TEAJF does not enforce the portion of Rule 6 stating that an attorney must consider whether a client's funds can generate net interest "without regard to the funds of other clients." *Id.* RULE 6.

*III. Standing*

Standing is a judicially-developed doctrine designed to ensure an Article III court is presented by parties before it with an actual case or controversy. *Lujan v. Defenders of Wildlife,* 504 U.S. 555, 561, 112 S.Ct. 2130, 119 L.Ed.2d 351 (1992) ("[S]tanding is an essential and unchanging part of the case-or-controversy requirement of Article III").

To establish standing, a party must allege a "personal injury fairly traceable to the defendant's allegedly unlawful conduct and likely to be redressed by the requested relief." *Id.* That injury must be "distinct and palpable and not abstract or conjectural or hypothetical." *Id.* (Internal quotes omitted). This injury requirement ensures that courts will decide only actual disputes and not abstract policy questions more properly decided by coordinate branches of government. *See, e.g., Allen v. Wright,* 468 U.S. 737, 746, 104 S.Ct. 3315, 82 L.Ed.2d 556 (1984) (stating that the law of Art. III standing is built on a single basic idea-the idea of separation of powers). Additionally, standing requires courts

to base decisions on a concrete, actual set of facts, so that a court may appropriately limit the precedential value of its decisions. *See Valley Forge Christian College v. Americans United for the Separation of Church and State,* 454 U.S. 464, 102 S.Ct. 752, 70 L.Ed.2d 700 (1982).

*A. To Whom Does the Money Belong?*

On February 4, 1994 Plaintiffs brought suit against Defendants based upon a $1000 retainer Mr. Summers paid his attorney Mr. Mazzone and his firm Dow Cogburn & Friedman P.C., ("Dow Cogburn"). This money was paid in May of 1993 in connection with civil litigation filed against Mr. Summers and Glenloch Homes in 1992.[1] Mr. Summers again paid a retainer of $250 to Mr. Mazzone in 1999 after this case was remanded by the Supreme Court.

Defendants argue that Mr. Summers does not have standing to bring this cause of action because the money placed in the Dow Cogburn IOLTA account did not belong to him, but to another entity, Abbey Enterprises. Defendants further assert that since this entity was a corporation, it could not earn interest on the $1000 retainer outside of IOLTA. Defendants assert that the Supreme Court holding that clients possess a property interest in the interest earned in an IOLTA account is based upon abstract principles of Texas property law and was not a factual determination that Mr. Summers possessed a property interest in the interest earned by the Dow Cogburn IOLTA account.

The evidence at trial established that the check with which Mr. Summers retained Mr. Mazzone in 1993 was not paid from his personal account, but from the account of a corporation, Abbey Enterprises. Transcript at 43. This

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[1] This case was dismissed in 1998 for want of prosecution. Transcript at 56.

money was placed under the client number for Glenloch Homes. Glenloch Homes was sued in conjunction with Mr. Summers, but was no longer in existence at the time the suit was filed. Transcript at 44, 111. The evidence established that Mr. Summers owned 60% of Abbey Enterprises and possessed the ability to write himself a check to pay his salary. Transcript at 114. Summers testified that he paid personal income taxes in 1993 on the $1000 he used to retain Mr. Mazzone. Transcript at 125. The evidence at trial further established that Abbey enterprises was not party to the litigation supported by the $1000 retainer.

Mr. Mazzone testified that four days prior to filing the instant suit in February of 1994, he instructed the bookkeeper at his firm to create a client number for Mr. Summers and to transfer the $1000 retainer from the Glenloch Homes client number to Mr. Summers' name. Transcript at 53, 84.

Plaintiff Summers maintains that this check, drawn on a corporate account was merely a distribution or salary payment to Mr. Summers and was treated as such on Abbey's books. Therefore, Plaintiffs argue that the money in issue was the property of Mr. Summers. Moreover, Plaintiffs argue that Summers paid Mr. Mazzone an additional retainer of $250 which Mr. Mazzone also placed in the Dow Cogburn IOLTA account. Transcript at 63. This check was written on Plaintiff's personal account. Plaintiffs' Trial Exhibits 13 and 14. Based on this, Plaintiffs assert that the ownership of the original retainer is irrelevant.

The Court finds that, for the purposes of this litigation, the $1000 retainer was the property of Mr. Summers sufficient to establish standing. *Heinrichs v. Evins Personnel Consultants, Inc., Number One,* 486 S.W.2d 935, 936 (1972). Moreover, even if the Court had not found that the $1000 is the property of Mr. Summers, it is clear the second retainer of $250 is Mr. Summers' personal property sufficient to support standing.

*B. Should the Money Ever Been Placed in IOLTA?*

Defendants argue that the $1000 retainer paid on the Abbey Enterprises account never should have been placed in an IOLTA account in the first place. The Court finds that pursuant to IOLTA Rule 6 Mr. Mazzone properly determined at that time that the money would not generate net interest. Transcript at 46. Mr. Mazzone testified that he was unaware of the TEAJF policy of refunding interest on funds inadvertently placed in an IOLTA account until "recently." Transcript at 59. Mr. Mazzone further testified that he did not believe he had placed the $1000 in IOLTA by mistake. *Id.* The Court finds that pursuant to the Rules governing IOLTA at the time Mr. Mazzone placed Mr. Summers' retainer funds in the IOLTA account, Mr. Mazzone properly placed the money in his firm's IOLTA account. The Court further finds that Mr. Mazzone's determination that the $250 retainer should be placed in IOLTA is also proper.

*C. Mr. Summers' Bankruptcy*

Defendants contend that due to a Chapter 7 bankruptcy filing, Mr. Summers cannot claim the benefit of the interest his funds allegedly earn in IOLTA. The testimony established that Mr. Summers filed for bankruptcy in June of 1999. Transcript at 61. The testimony further established that at this time, Mr. Summers owed the firm of Dow, Cogburn & Friedman in excess of $1000 in unpaid legal fees. Transcript at 119.

In light of Mr. Mazzone's continued representation of Mr. Summers, the Court finds that the retainer is still the property of Mr. Summers held in trust by Mr. Mazzone. Although Mr. Mazzone's failure to apply the $1000 retainer to an outstanding bill is somewhat unorthodox, his choice not to do so will not be questioned by this Court at this juncture. No evidence was submitted to this Court that any creditor of Mr. Summers laid claim to the $1000. Mr. Summers also testified that he informed the bankruptcy trustee of the

existence of the $1000 retainer. Transcript at 120. Therefore, the Court finds that the nature of the ownership of $1000 retainer cannot be re-characterized by Mr. Summers' bankruptcy.

*IV. Failure to Join an Indispensable Party*

*A. Special v. General Accounts*

Defendants argue that this Court should reconsider the Supreme Court's determination that a client has a property interest earned on money placed in an IOLTA account. Defendants contend that the Supreme Court's decision was based on the assumption that the client owned the principal. Defendants contend that the Supreme Court "implicitly assumed" that IOLTA accounts are special in nature. In fact, Defendants assert, IOLTA accounts are general accounts, and the bank owns the principal instead of the client. *Texas Commerce Bank v. Townsend,* 786 S.W.2d 53 (Tex.App.–Austin 1990, writ denied).

In Texas, accounts are assumed to be general accounts unless the parties can establish that the account was a special account under an agreement with the bank that those particular deposits would be kept separate from the banks other funds. *Id.* There is no evidence that the parties at any time attempted to establish that the IOLTA account in issue was a special account.

In a special account, the depositor retains an interest in the specific principal placed on deposit. In a general account, all ownership rights in the principal are transferred to the financial institution and a debtor-creditor contractual relationship is established. *Hudnall v. Tyler Bank & Trust Co.,* 458 S.W.2d 183, 186 (Tex.1970).

Mr. Mazzone testified that the Dow Cogburn trust account was a general account. Transcript at 54. Mr. Mazzone further testified that he understood that in a general account his firm only had the contractual right to be repaid a

sum equal to the original deposits in that account. Transcript at 90. The Court finds that the Dow Cogburn IOLTA account is and was a general account.

The Court finds that the Supreme Court's finding was not based on an assumption that IOLTA accounts are special in nature. In *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980), which the Supreme Court relied largely upon in coming to its determinations in *Phillips,* the account in issue was an interest-bearing general account and not a special account. In fact, in most cases a special account is not an interest-bearing account. *See* Testimony of Karen Neeley, Transcript at 363-64. As a matter of common sense, a bank would not pay interest on funds it could not use. Therefore an IOLTA account would not be feasible as a special account. The Court finds that Defendants' assertion that the Supreme Court assumed IOLTA accounts are special accounts is without merit. Therefore the Court declines to reconsider the property interest issue on this basis.

*B. Banks as Indispensable Parties*

Defendants assert that in a general account Texas law states that the financial institution holds title to the funds deposited. *Paulsen et al v. Texas Equal Access to Justice Foundation,* 1999 WL 1078698, No. 03-98-00709-CV (Tex.App.–Austin, Dec. 2, 1999, n.w.h.). Therefore, based upon the legalism "interest follows principal" the banks in which Mr. Mazzone's law firm maintained it IOLTA accounts relevant to this cause of action-Chase Bank of Texas and Southwest Bank of Texas-hold title to the interest generated by IOLTA as well as the funds. Defendants request this Court to dismiss this cause of action pursuant to Fed.R.Civ.P. 19(a)(1), for failure to include the banks as indispensible parties. The Court finds this argument must fail.

The Rule provides that a party is "necessary" and "shall be joined" if:

> (1) in the person's absence complete relief cannot be accorded among those already parties, or (2) the person claims an interest relating to the subject of the action and is so situated that the disposition of the action in the person's absence may (i) as a practical matter impair or impede the person's ability to protect that interest or (ii) leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of the claimed interest.

Fed.R.Civ.P. 19(a). "A decision whether to dismiss must be made pragmatically, in the context of the substance of each case, rather than by procedural formula." *Provident Tradesmens Bank & Trust Co. v. Patterson,* 390 U.S. 102, 119, n. 16, 88 S.Ct. 733, 19 L.Ed.2d 936 (1968).

The Court finds, after carefully considering all the factors set forth in Rule 19(a), that Chase Bank of Texas and Southwest Bank of Texas are not necessary parties to this cause of action. First, in the absence of these parties, Plaintiffs can be afforded complete relief. They request injunctive relief only. An order enjoining TEAJF from applying the IOLTA program to Plaintiffs would provide them with complete relief.

In the alternative, failure to join these financial institutions would not "as a practical matter impair or impede the person's ability to protect" the banks' interest in IOLTA accounts. Mr. Mazzone contracted with these banks to pay the interest generated by his firm's IOLTA account to TEAJF. *See* Plaintiff's Exhibit 6, Affidavit of Professor Rounds. Certainly, a necessary change in this contractual relationship by the injunction of IOLTA will not impede the

banks' interest. In fact, it might be in the banks' better interests to retain the interest on these accounts as they did pre-IOLTA. Lastly, failure to join the banks would not "leave any of the persons already parties subject to a substantial risk of incurring double, multiple, or otherwise inconsistent obligations by reason of the claimed interest." Fed.R.Civ.P. 19. Obviously, because Plaintiffs seek only declaratory and injunctive relief, failure to join these financial institutions would not leave the other Defendants open to multiple obligations. The Court finds that these financial institutions are not necessary parties to this litigation. Therefore, the Court denies Defendants' motion to dismiss on this basis.

*V. First Amendment*

Plaintiffs allege that Texas' mandatory IOLTA program violates Plaintiffs' First Amendment rights by forcing them to finance speech they find objectionable. Plaintiffs originally asserted these claims before the district court in *Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 873 F.Supp. 1 (W.D.Tex.1995). In that opinion, this Court found that Plaintiffs' First Amendment claims "at least as far the client is concerned . . . is necessarily predicated upon the Plaintiffs' claim that the funds generated by the IOLTA accounts are, in fact, the property of the client." *Id.* at 9. This Court further found that:

> the IOLTA Program in no way compels any of the Plaintiffs to actually associate or otherwise be linked with the recipient organizations that they find repugnant (*e.g.* by becoming members or being publicly listed as benefactors). Because the Plaintiffs have failed to adequately allege any connection between themselves and the IOLTA recipient organizations, the Court finds that the Texas

IOLTA Program does not unconstitutionally burden the Plaintiffs' First Amendment rights.

*Id.*

Neither the Fifth Circuit nor the Supreme Court directly addressed Plaintiffs' First Amendment challenge to IOLTA.[2] However, to the extent that this court's earlier opinion is premised upon the finding that the interest generated by the IOLTA funds qualifies as "property" the Court revisits the First Amendment issue.

*A. Compelled Speech*

Plaintiffs assert that the Texas IOLTA Program compels them to speak in violation of the First Amendment. The Supreme Court has acknowledged in two distinct lines of cases, two counterparts to the First Amendment's guarantee of free speech: the right not to speak, *West Virginia State Board of Education v. Barnette,* 319 U.S. 624, 642, 63 S.Ct. 1178, 87 L.Ed. 1628 (1943); and the right not to be compelled to subsidize others' speech, *Abood v. Detroit Bd. of Educ.,* 431 U.S. 209, 97 S.Ct. 1782, 52 L.Ed.2d 261 (1977); *Keller v. State Bar of Cal.,* 496 U.S. 1, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990). The first line of cases involves individuals being required to engage in involuntary affirmations of public belief. *See Wooley v. Maynard,* 430 U.S. 705, 714, 97 S.Ct. 1428, 51 L.Ed.2d 752 (1977) (displaying a government motto); *West Virginia State Board of Education v. Barnette,* 319 U.S. 624, 642, 63 S.Ct. 1178, 87 L.Ed. 1628 (1943) (pledging allegiance to the flag). The second line of cases involves compelled financial support of private organizations. *Abood v. Detroit Bd. of Educ.,* 431

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[2] Plaintiffs assert that the Fifth Circuit's opinion that the grant of summary judgment was reversed in its entirety and therefore Plaintiffs' First Amendment claims have been fully revived. *See* Plaintiffs' Motion for Summary Judgment at 11.

U.S. 209, 97 S.Ct. 1782, 52 L.Ed.2d 261 (1977), and *Keller v. State Bar of California,* 496 U.S. 1, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990). Plaintiffs rely on these two lines of Supreme Court cases in support of their arguments.

*B. The Right Not to Speak*

Defendants assert that a compelled speech cause of action requires a showing that the Plaintiff[3] will be identified with the message he finds objectionable and that Plaintiff cannot do so in the instant case. The Court finds that Defendants are correct with regard to the *West Virginia State Board of Education v. Barnette* line of cases. Plaintiffs agree that this line of cases requires that Plaintiffs show that they are being identified with the expressive activity to which they object. *See PruneYard Shopping Center v. Robins,* 447 U.S. 74, 87-88, 100 S.Ct. 2035, 64 L.Ed.2d 741 (1980).

In *PruneYard,* the Supreme Court sustained a California law requiring the proprietors of shopping malls to allow visitors to solicit signatures on political petitions. The Supreme Court based that decision at least in part upon the fact that the solicitations would "not likely be identified with those of the owner," and that "no specific message is dictated by the State to be displayed on appellants' property." Moreover, the proprietors could "expressly disavow any connection with the message by simply posting signs in the area where the speakers or handbillers stand." *Id.* at 87, 100 S.Ct. 2035.

At trial Mr. Summers testified that he did not believe that the people of the State of Texas identified him with the causes funded by TEAJF with IOLTA funds. *See* Transcript

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[3] Plaintiffs have abandoned their claim that Mr. Mazzone's First Amendment rights are being violated by mandatory participation in IOLTA. *See* Trial Transcript at 51.

at 116. The Court finds that no specific message is dictated by the variety of legal services that TEAJF funds with IOLTA dollars. Moreover, the Court finds Summers is free to publicly disassociate himself with the views of any IOLTA-funded litigation with which he disagrees. In fact, to a limited extent he has done so by filing this cause of action.

The relationship between Mr. Summers, Mr. Mazzone, IOLTA, the TEAJF, and the programs funded by the TEAJF with IOLTA funds is not easily traceable. Mr. Summers admitted that his money was placed in the Dow Cogburn IOLTA account long before he was aware of the existence of IOLTA, let alone the causes funded by IOLTA. *See* Transcript at 51, 112. No evidence was submitted at trial of any identification of Mr. Summers with the programs funded with IOLTA monies. Therefore the Court finds that Summers has failed to establish that he is being identified with the expressive activities to which he objects and any claim premised upon this fails based upon the dictates of *PruneYard.*

*C. Compelled Financial Support*

Plaintiffs are still free to assert that they prevail under the compelled financial support line of cases. *Abood v. Detroit Bd. of Educ.*, 431 U.S. 209, 97 S.Ct. 1782, 52 L.Ed.2d 261 (1977); *Keller v. State Bar of Cal.*, 496 U.S. 1, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990). Pursuant to these cases, Plaintiffs argue that the Texas IOLTA Program violates the First Amendment's prohibition on compelled speech by forcing Mr. Summers to financially support private organizations to which he objects. Plaintiff Summers objects on ideological grounds to the use of his funds to support IOLTA. *See* Transcript at 116.

Taken as a whole, the compelled contribution line of cases require a showing of three factors. First there must be an involuntary contribution. *Abood,* 431 U.S. 209, 97 S.Ct. 1782, 52 L.Ed.2d 261 (1977). Second, the message

supported by the involuntary contribution must be political or ideological. *Keller,* 496 U.S. 1, 9-17, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990). Third, even when the message supported by the involuntary contribution is political or ideological, no First Amendment violation exists if the message supports the government's policy interests. *Id.*

The Court notes that "the government does not, however, violate the First Amendment whenever it forces an individual to subsidize speech." *Hays County Guardian v. Supple,* 969 F.2d 111, 123 (5th Cir. 1992). "Rather, the First Amendment prohibits the government from forcing an individual to contribute to the ideological expression of other private citizens for the purpose of advancing those citizens ideological biases rather than substantial public interests." *Id.*

*1. Compelled Involuntary Contribution*

Defendants argue that Plaintiff Summers was not required to make an actual financial contribution, such as union dues, *Abood v. Detroit Board of Educ.,* 431 U.S. 209, 97 S.Ct. 1782, 52 L.Ed.2d 261 (1977), or bar dues, *Keller,* 496 U.S. 1, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990), to the IOLTA Program. Defendants argue that therefore Plaintiffs cannot maintain the argument of compelled financial support. Defendants maintain that in this case, the client made no financial contribution at all. Defendants assert that without the IOLTA Program Plaintiff Summers' money would have gone into a non-IOLTA account with the interest benefitting only the bank.

Defendants further contend that Plaintiff Summers was not "compelled" to contribute to IOLTA because the client has already voluntarily relinquished all beneficial use of his money to the bank. *PruneYard Shopping Center v. Robins,* 447 U.S. 74, 87-88, 100 S.Ct. 2035, 64 L.Ed.2d 741 (1980). Defendants assert that the State is not requiring the client to contribute anything that he has not already given up.

Plaintiffs argue that Mr. Summers' participation in IOLTA is not voluntary. They correctly assert that since Mr. Summers was not even aware of IOLTA for nearly a year following the placement of his funds in an IOLTA account, he could not have consented to participation. Transcript at 112. Defendants' assertion of voluntariness is premised on the fact that Mr. Summers willingly turned over the $1000.00 retainer to his attorney. Plaintiffs maintain that Defendants' assertion is incorrect as a matter of constitutional law. Plaintiffs assert that this case is akin to the finding that a state cannot condition employment in a government job on public support of a political party. The First Amendment is violated even though the plaintiff may avoid the compelled speech by refusing to accept the proffered job. *Elrod v. Burns,* 427 U.S. 347, 96 S.Ct. 2673, 49 L.Ed.2d 547 (1976).

The issue of voluntariness in this case is highly related to this Court's findings regarding the ability of Mr. Summers' funds, placed in the Dow Cogburn IOLTA account, to generate interest that would equate to a measurable contribution. *Lehnert v. Ferris Faculty Ass'n,* 500 U.S. 507, 111 S.Ct. 1950, 114 L.Ed.2d 572 (1991). For the sake of Plaintiffs' First Amendment claims, the Court will assume that Mr. Summers was required to involuntarily contribute to IOLTA.[4]

*2. Ideological or Political Activity*

Plaintiffs contend that the activities funded by TEAJF are ideological and/or political in nature. Plaintiffs assert that the advocacy of legal rights is by its very nature an inherently expressive activity and thus is subject to the compelled

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[4] The Court notes the Defendants' contention that an attorney and client may both avoid placing funds in IOLTA by "creative" structuring of the financial relationship. Mr. Mazzone required that Mr. Summers pay a retainer but he could have chosen an alternative form of payment.

speech doctrine. *Lehnert v. Ferris Faculty Assoc.*, 500 U.S. 507, 111 S.Ct. 1950, 114 L.Ed.2d 572 (1991). Plaintiffs further argue that IOLTA funds have been expended to finance a lawsuit by a group of Democrats seeking to overturn the election results in Val Verde County, Texas[5] and to assist illegal aliens resisting deportation. Transcript at 211-212. Plaintiffs maintain that these are ideological and/or political activities to which Mr. Summers objects.

Defendants argue that the Texas IOLTA Program does not support a discernable message. Moreover, Defendants argue that a compelled contribution violates the First Amendment only where the "dissenter's objection rests on political or ideological disagreement with the content of the message." *Glickman v. Wileman Bros. & Elliott,* 521 U.S. 457, 471, 117 S.Ct. 2130, 138 L.Ed.2d 585 (1997). Defendants argue that Mr. Summers has failed to identify the message propounded by the TEAJF with IOLTA funds, with which he disagrees.

At issue in this case is whether Plaintiff Summers objects to certain programs supported with IOLTA funds or whether he objects to the very existence of the IOLTA Program. The Court finds that Mr. Summers' objections to certain programs are a vehicle for his general objections to IOLTA. Mr. Summers does not object to the use of IOLTA funds because it creates a "crisis of conscience;" but rather, because he simply objects to the TEAJF's control over the IOLTA funds. *See Glickman v. Wileman Bros. & Elliott,* 521 U.S. 457, 471, 117 S.Ct. 2130, 138 L.Ed.2d 585 (1997). The concept of helping ensure equal access to the justice system for low income citizens is in itself a non- controversial idea,

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[5] The TEAJF submits that no IOLTA funds were earmarked for this litigation and that TEAJF restricts the use of IOLTA money through the terms of the grant.

*Logan v. Zimmerman Brush Co.*, 455 U.S. 422, 102 S.Ct. 1148, 71 L.Ed.2d 265 (1982), and therefore does not qualify as a political or ideological activity. *Hays County Guardian v. Supple*, 969 F.2d 111 (5th Cir.1992). To the extent that Mr. Summers complains that the IOLTA Program is in itself expressive activity his claim fails. However, the Court finds that the TEAJF's activities in funding certain litigation could be ascribed certain political or ideological components and therefore potentially qualify as expressive activity against which Plaintiffs may lodge a First Amendment claim. The Court finds that Plaintiffs' First Amendment claims nevertheless fail.

*3. Core Government Function*

Defendants assert that the Texas IOLTA Program supports a core government function by providing access to the Texas justice system.

In *Abood*, the Supreme Court addressed the First Amendment claims of dissenting employees subject to an "agency-shop" agreement between their government and a union. The agreement required each employee to pay the union a "service fee" equal to the dues required of union members, but limited no one's right to speak separately and obliged no employee to join the union, personally espouse unionism, or participate in the union in any other way. *Abood v. Detroit Board of Education*, 431 U.S. 209, 97 S.Ct. 1782, 52 L.Ed.2d 261 (1977). The Supreme Court found in that case that the union's use of the dissenter's service fees for expressive purposes unrelated to collective bargaining violated the First Amendment rights of those employees. *Abood* struck down the service fee because it funded the union's expression of support for "ideological causes not germane to its duties as collective bargaining representative." *Id.* at 235, 97 S.Ct. 1782.

In *Glickman v. Wileman Brothers & Elliott, Inc.*, the Supreme Court solidified its holding in *Abood* and stated that:

> the Court reads *Abood* for the proposition that the First Amendment places no limits on government's power to force one individual to pay for another's speech, except when the speech in question is ideological or political in character and is not germane to an otherwise lawful regulatory program.

521 U.S. 457, 471-472, 117 S.Ct. 2130, 138 L.Ed.2d 585 (1997).

Therefore, the question now before the Court is whether the IOLTA Program itself and the expressive activity that Mr. Summers objects to the TEAJF funding are germane to an otherwise lawful regulatory program and support a substantial public interest-that of supplying legal services to the poor. *Hays County Guardian v. Supple,* 969 F.2d 111 (5th Cir.1992). The Court finds that the compelled contribution of Plaintiff's funds to IOLTA accomplishes and is germane to the "government's vital policy interest" of making legal services accessible to all. *Lehnert v. Ferris Faculty Ass'n,* 500 U.S. 507, 111 S.Ct. 1950, 114 L.Ed.2d 572 (1991). "Improving the quality of legal services" is an important state interest. *Keller v. State Bar of Cal.,* 496 U.S. 1, 7, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990) (citing *Lathrop v. Donohue,* 367 U.S. 820, 81 S.Ct. 1826, 6 L.Ed.2d 1191 (1961)). Plaintiffs have failed to identify any instance where TEAJF funds were used in a manner not consistent with providing access to legal services. Unlike in *Keller,* the TEAJF has not used IOLTA funds to lobby or in an attempt to legislate. The Court finds that compelled funding of IOLTA does not "significantly add to the burdening of free speech." *Lehnert,* 500 U.S. at 521, 111 S.Ct. 1950. Moreover, "[t]he reason for permitting the government to

compel the payment of taxes and to spend money on controversial projects is that the government is the representative of the people." *See Abood,* 431 U.S. at 259, n. 13, 97 S.Ct. 1782 (Powell, J., concurring in judgment).

The sole purpose of the TEAJF is to fund legal services for the poor. Its activities in funding various programs are germane to this government interest. Based on the foregoing, the Court finds that Plaintiffs' First Amendment claims must fail.[6]

*VI. Fifth Amendment*

Having addressed Plaintiffs' First Amendment claims, the Court now turns to the central issue in this case – whether or not a taking occurred pursuant to the Fifth Amendment and if so, what is the just compensation for that taking.

The Fifth Amendment provides that "private property" shall not be "taken for public use without just compensation." U.S. CONST., amend. V. To prove an unconstitutional taking, Plaintiffs must first establish that a cognizable property right exists in the thing taken-in this case

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[6] The Court is prepared to determine if the IOLTA program is narrowly tailored to the compelling state interest of making legal services accessible to all citizens. However, the parties seem to have abandoned any claims of this nature. *See* Parties' Agreed Pre-Trial Order. The Court finds that IOLTA is a content neutral program. *See* Plaintiffs' Motion for Summary Judgment at 17. Therefore an intermediate level of scrutiny is applicable. *United States v. O'Brien,* 391 U.S. 367, 377, 88 S.Ct. 1673, 20 L.Ed.2d 672 (1968). In this case, it seems clear that IOLTA furthers an important government interest, unrelated to the suppression of free speech, and the incidental burdens on First Amendment freedoms is no greater than is essential to the furtherance of that interest. *Id.* The government's interest in making legal services accessible would be achieved less effectively absent the existence of IOLTA. *Ward v. Rock Against Racism,* 491 U.S. 781, 791, 109 S.Ct. 2746, 105 L.Ed.2d 661 (1989).

the interest earned on client funds placed in IOLTA accounts. *See Penn Central Transp. Co. v. City of New York*, 438 U.S. 104, 124-25, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978). The United States Supreme Court determined that the interest income held in IOLTA accounts is the "private property" of the owner of the principal. The Court stated:

> We express no view as to whether these funds have been "taken" by the State; nor do we express an opinion as to the amounts of "just compensation," if any, due respondents. We leave these issues to be addressed on remand.

*Phillips v. Washington Legal Foundation*, 524 U.S. 156, 118 S.Ct. 1925, 1934, 141 L.Ed.2d 174 (1998). Thus the Court must address these issues on remand.

The parties to this cause of action have stipulated, and the United States Supreme Court has recognized, that during the period of this litigation, from 1994 to the present, Texas lawyers were permitted under the IOLTA rules to pool client trust funds into a single account; either a IOLTA or non-IOLTA savings or NOW account that generated net interest for clients. *See* Pre-trial Order at 7.

"The Fifth Amendment does not proscribe the taking of property; it proscribes taking without just compensation." *Williamson County Regional Planning Comm'n v. Hamilton Bank of Johnson City*, 473 U.S. 172, 194, 105 S.Ct. 3108, 87 L.Ed.2d 126 (1985). The Court addresses the issue of just compensation first.

*A. Just Compensation*

Regardless of the Court's determination of whether a taking occurred, the crux of this case rests on the issue of just compensation. "As its language indicates, and as the Court has frequently noted, [the Takings Clause] does not prohibit the taking of private property, but instead places a condition on the exercise of that power. This basic understanding of

the Amendment makes clear that it is designed not to limit the governmental interference with property rights per se, but rather to secure compensation in the event of otherwise proper interference amounting to a taking." *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles,* 482 U.S. 304, 314-315, 107 S.Ct. 2378, 96 L.Ed.2d 250 (1987). Of all the terms used in the Takings Clause, "just compensation" has the strictest meaning. The Fifth Amendment does not allow simply an approximate compensation but requires "a full and perfect equivalent for the property taken." *Monongahela Navigation Co. v. United States,* 148 U.S. 312, 326, 13 S.Ct. 622, 37 L.Ed. 463 (1893).

In determining just compensation, "the question is what has the owner lost, not what has the taker gained." *Boston Chamber of Commerce v. Boston,* 217 U.S. 189, 195, 30 S.Ct. 459, 54 L.Ed. 725 (1910). The government is not obligated to compensate a property owner for a "loss of theoretical creation, suffered by no one in fact." *Id.* at 194, 30 S.Ct. 459. "Just compensation" generally means "the full monetary equivalent of the property taken." *United States v. Reynolds,* 397 U.S. 14, 16, 90 S.Ct. 803, 25 L.Ed.2d 12 (1970) at 194. In determining the amount of just compensation for a taking, a court seeks to place a claimant "in as good a position pecuniarily as if his property had not been taken." *United States v. 564.54 Acres Land,* 441 U.S. 506, 510, 99 S.Ct. 1854, 60 L.Ed.2d 435 (1979) (quoting *Olson v. United States,* 292 U.S. 246, 255, 54 S.Ct. 704, 78 L.Ed. 1236 (1934)). The Court must calculate any loss objectively and independently of the claimant's subjective valuation. *See, e.g., Kimball Laundry Co. v. United States,* 338 U.S. 1, 5, 69 S.Ct. 1434, 93 L.Ed. 1765 (1949).

The factual issue before the Court in deciding what award would be needed to place Mr. Summers in as good a position as he would have enjoyed without the alleged taking, is what is the monetary amount of the net interest or

net benefit lost by Mr. Summers because his funds were placed in IOLTA. The Court will measure any required compensation by Mr. Summers' loss, not by the government's gain, or in this case the gain enjoyed by the recipients of TEAJF funding.

Plaintiffs argue that the value taken in this case is easily ascertainable. Whatever the amount of interest earned by Mr. Summers' monies, regardless of expenses incurred to generate the interest, is the amount of Mr. Summers' just compensation. Mr. Summers testified at trial that he was no worse off because of IOLTA. Transcript at 136. Additionally, this evaluation would only be appropriate if the Court applies a per se analysis, which the Court declines to do.

Plaintiffs assert in this case that although a client's money placed in an IOLTA account cannot garner net interest without IOLTA it could still tally a net benefit to the client. Plaintiffs assert that the costs that a lawyer must consider when placing funds in her IOLTA account are incorrectly distributed. In determining whether to place funds in an IOLTA account a lawyer is asked to consider internal costs: the expense of the attorney's or law firm's staff time in establishing a separate account; the expense of preparing and filing IRS forms, (1099's); the bookkeeping and accounting expenses for tracking the account; the monthly reconciliation of the account for the client; and, the closing of the account at the bank and remitting the funds to the client. A lawyer is also directed to consider the following external costs: the minimum balance at the bank at which the account is placed; the service charges, if any, assessed against the account by the bank; and other additional fees that the bank may have for investment policies. *See* Defendants' Exhibit 1.

Plaintiffs argue that the internal costs are costs the lawyer or firm will incur regardless of whether the funds are

placed in an IOLTA or non-IOLTA account. Plaintiffs argue that client funds can generate a net benefit to the client when not placed in IOLTA. The Court finds that the testimony at trial established otherwise. There are innate costs to the firm or lawyer in a non- IOLTA account that differ from those in an IOLTA account. The Court carefully considered the various evidence presented at trial regarding in-firm pooling, sub-accounting, and the net benefit theory. In light of the evidence before the Court, the Court finds that Mr. Summers did not suffer a compensable loss.

*1. In-Firm Pooling*

Plaintiffs offered the testimony of Robert Randell at trial. Mr. Randell is an attorney in New York who has established an in-firm pooling method for his own solo practice. Mr. Randell testified that he possesses a computerized system of linked ledger sheets that makes in-firm pooling inexpensive to the lawyer and beneficial to clients. Mr. Randell testified that he places all escrow deposits in a money market account. This includes corporate funds which cannot be placed in a NOW account unless the interest is paid to a charitable organization. Mr. Randell makes no initial determination whether the money is capable of earning net interest on its own, but places all client monies in the same fund. *See* Transcript 142-154. Plaintiffs offered Exhibit 24 which shows two accounts belonging to Mr. Randell's clients. This evidence illustrates Mr. Randell's method of calculating interest and fees. Mr. Randell testified that after the bank notifies him of the interest earned on the account, he apportions the interest to each client. He then charges an administrative fee which is about one-half of the interest earned, or in his characterization, one percent of the client's interest plus principal. Mr. Randell testified that he rarely has the funds of more than six clients in his account. He also testified that in his own practice there are times when he does not place client funds in an interest-bearing account

because it is too little money or for too short a period of time to gain a net benefit for the client.

The Court finds that Texas lawyers can make benefit of this process if it earns net interest for the clients. In fact, to do so is mandated by IOLTA. Tx. R. Equal Access Rule 4B (West 1999). However, the funds described in Mr. Randell's in-firm pooling scenario are funds that in most cases would earn a net benefit for the client without in-firm pooling. Moreover, Mr. Randell's allocation of the administrative fee by percentage of the client's money changes the ultimate determination of net interest. Seemingly, the administrative costs of allocating $2000 should not be less than those for the of allocation $200,000. In Mr. Randell's scheme, the larger dollar amounts in his "pool" in effect pay the costs for the smaller amounts and allow those smaller amounts to earn interest. There may be net interest on the smaller accounts but only at a loss to the larger. This system would only affect a small percentage of money that otherwise would be placed in IOLTA and fails to address small amounts of money held for short periods of time that could not earn interest at all. Mr. Randell's unique situation, where he deals with a small number of transactions, larger amounts of money, and over lengthy time periods is not illustrative for purposes of any determination regarding IOLTA. IOLTA requires the attorney to make an initial determination of whether the client funds can earn net interest. In cases where the funds can earn net interest, the attorney is to place the funds in an appropriate financial product. Only in such cases would Mr. Randell's in-firm pooling arrangement be feasible. Even in these cases, Mr. Randell is subsuming the bank's role in an effort to generate an added administrative fee for his practice, albeit with the agreement of his clients. Added to this, Mr. Randell must prepare the 1099 forms for each client earning in excess of $10 in interest. Moreover, Mr. Randell's system is not a demand account as mandated by the rules of ethics. Tex.

Disciplinary R. Prof. Conduct 1.14, *reprinted in* Tex. Gov't Code Ann., tit 2, subtit. G app. A (Vernon's Supp.1998) (Tex. State Bar R. Art. X, § 9). The Court finds that Plaintiffs have failed to establish that Mr. Summers' monies could earn net interest if placed in an in- firm pooled account.

*2. Sub-accounting*[7]

Plaintiffs offered evidence at trial in an effort to establish that client monies could earn net interest through sub-accounting practices. Sub- accounting is a banking product where an entity such as a law firm opens a master account in its name and a linked sub-account for each client for whom the firm is holding funds. Defendants' Exhibits 42 and 43. These sub- accounts are interest bearing accounts with the interest rate aligned with that earned in a money market account. In the Chase Client Funds Account, which Plaintiffs offer as an example of the service, the bank provides a monthly report to the attorney or firm tracking every disbursement, and interest earned in each sub-account. The bank also prepares IRS 1099 forms at the end of the year for each sub-account. Chase advertises this product as "specifically suited to high balance, low activity, escrow funds management." The monthly fee is $21.00 if the balance is below $5,000; $15 if the balance is between $5000 and $14,999; and $10 if the balance is between $15,000 and $39,999. Additionally, the bank charges activity fees for almost all transactions. These fees vary from $.20 for a deposited check to $25.00 for a daily report by fax on five

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[7] The parties presented a multiplicity of evidence at trial in an effort to determine whether sub-accounting is in fact available in Texas. The Court finds that at this point in time sub-accounting is not available in Texas. *See* Testimony of Karen Neeley and Frank Newton. However, a lawyer could in theory, and with his client's agreement, open a sub-account outside of Texas. *See* Transcript at 209. Nevertheless, the Court finds that this issue is irrelevant to this cause of action.

accounts. The evidence establishes that the Citibank sub-accounting product charges similar fees, but that Citibank offers a no fee business account as long as the average balance exceeds $1000. However, it is not clear from the evidence offered at trial the terms and conditions of this particular type of account.

Mr. Randell testified as to the availability of bank sub-accounting products in the state of New York. *See* Plaintiffs' Exhibits 21, 22, and 23. These exhibits are advertisements demonstrating the availability sub-accounting products in New York by Chase and Citibank. None of these advertisements discuss the costs of sub-accounting products. Mr. Randell further testified that nothing in the IOLTA rules prohibits the use of bank sub-accounting products. Transcript at 179. On cross-examination, Mr. Randell testified that with regard to the sub-accounting products offered by Chase, if the client account is zero for ten consecutive days, the account would be closed and the interest forfeited. Transcript at 184; Defendants' Exhibit 42, Terms and Conditions for Business Accounts and Services at 16.

A lawyer using this product is limited to three withdrawals by check per month and may make an additional three transfers by telephone, computer, pre- authorized third party payments, and pre-authorized transfers to another account. Transactions exceeding these limits are charged banking fees. There is no limit on the number of withdrawals or transfers made; in-person, by mail, by messenger, or at an ATM.

Claude Ducloux, a solo practitioner from Austin Texas, testified about the operation of his IOLTA account. Mr. Ducloux testified to the following: that IOLTA costs to an individual attorney operating an IOLTA account are zero, *see* Transcript at 269-270; that on average he keeps the funds of 20-30 clients in his account in the amount of $20,000 to

$30,000; that he keeps most of the client funds in the account for 30 to 60 days and garners an interest rate of 72 hundredths of one percent, Transcript at 272; that his IOLTA account earns less than $15 in interest per month; that transactional fees and internal costs in his own time would make apportioning this $15 interest among his 25 clients a net loss; that in the month of August 1999 he had a net interest of $10 on the $32,000 in his non-IOLTA firm account and bank charges of $12.

Ducloux also testified to the following: that for sub-accounting to be feasible for his use the product would have to be free and that would not take into account his time spent reconciling the account; that included in his expenses of allocating interest would be determining the date the check clears, the interest rate, deductions for any transactions using the client money, and recalculations of interest, Transcript at 277; that if in-firm pooling software were available he would still have the costs of buying the software and inputting the data; and that it requires five minutes for him to reconcile his IOLTA account each month.

Plaintiffs assert that reconciliations like Mr. Ducloux's still have a cost and that cost is passed on to the client. Dean Frank Newton testified that many Texas firms do not consider their own overhead when determining whether to place funds in IOLTA. Transcript at 223. Therefore some funds are not placed in IOLTA that theoretically should be placed in IOLTA under the rules. Dean Newton also testified that prior to the institution of IOLTA, these same funds did not earn interest. Transcript at 217.

Karen Neeley, general counsel for the Independent Bankers' Association of Texas testified that banks in Texas are not offering sub-accounting because such products are too expensive for the banks. Transcript at 331. Ms. Neeley testified to the following: that it is time consuming for banks

to set up each sub-account; that bank charges are generally on the increase, Transcript at 336; that in her opinion, in many cases the use of sub-accounting would result in a net of less than zero, Transcript at 343; and that the termination of the IOLTA program would not result in the advent of sub-accounting availability in Texas, but the pre-1984 status quo where lawyers' trust accounts earned no interest.

Ms. Neeley also testified to the following: that a demand account may not offer interest; that a NOW account and a savings account are not demand accounts, Transcript at 360; and that many banks waive fees for IOLTA accounts, but that some banks still charge these fees. Transcript at 362.

Mr. Bruce Buell, a solo practitioner from Colorado with a specialization in banking and trust and estate law testified that after NOW accounts were authorized in 1980, the IRS ruled that if interest earned on NOW accounts went to IOLTA there was no tax liability for individual clients. This was because the client had no authority to determine where the money was allocated.

Mr. Buell also testified that under the current IOLTA program attorneys can place client monies that they determine cannot earn net interest in an IOLTA account or, if the attorney determines that the client's money can earn net interest, in a separate NOW account, separate savings account, in-firm pooling, or sub-account. Transcript at 384-86.

Mr. Buell also testified to the following: that in his opinion, sub-accounting is appropriate only for higher balance accounts with less activity, Transcript at 389; that IOLTA accounts are cheaper in bank service charges and cost less in attorney time than non-IOLTA accounts, Transcript at 401; that in IOLTA accounts, the TEAJF pays the service and maintenance fees so there is no charge to the attorney, Transcript at 397; that generally banks do not require minimum balances on IOLTA accounts, there are no

restrictions on transfers or withdrawals, and that there is one monthly reconciliation, Transcript at 398; that sub-accounts will have maintenance and service fees, minimum balances, restrictions on transfers and withdrawals, and monthly reconciliations for the master account and each sub-account; that the man-hour time in reconciling the accounts as well as tracking transfers would be significant, Transcript at 399; and that separate accounts for each client would be more expensive that sub-accounts, but that the costs in man hours for the attorney would be similar. Transcript at 400.

Lastly, Mr. Buell testified that the costs to the lawyer of maintaining a sub- account are much greater than those of maintaining an IOLTA account. Therefore, the costs of maintaining an IOLTA account are not passed to the clients, while the costs or maintaining a sub-account would. Transcript at 418. Moreover, Mr. Buell testified that since the TEAJF bears the costs of maintaining IOLTA accounts, these accounts are less expensive to administer than other alternatives. Transcript at 396.

The Court finds that the costs of sub-accounting in lawyer and staff hours and in addition to bank charges exceed the costs of IOLTA. These costs make net interest to clients infeasible except in cases where large sums of money are held or when client funds are held for long periods of time. In these cases, the client funds would not be placed in IOLTA. Therefore, the Court finds that Plaintiffs' have failed to establish through the evidence before the Court that Mr. Summers' funds could theoretically earn net interest in a sub-account.

*3. Net Benefit Theory*

Plaintiffs offer the theory that even if Plaintiffs' money cannot generate net interest for the client, the money can attain a net benefit for the client. This theory is difficult to fathom, but in a nutshell is that by decreasing the lawyer's costs through use of the client's money, the client will

benefit. Although this may be true to an extent, this option is generally foreclosed by Cannon 11 of the Canon of Professional ethics. *See* Plaintiff's Exhibit 16, and specifically by the applicable ethical rules.

Canon 11 provides:

> A lawyer should refrain from any action whereby for his personal benefit or gain he abuses or takes advantage of the confidence reposed in him by his client. Money of the client or collected for the client or other trust property coming into possession of the lawyer should be reported and accounted for promptly, and should not under any circumstances be commingled with his own or be used by him.

Texas State Bar Rule of Professional Conduct 1.14 provides:

> (a) A lawyer shall hold funds and other property belonging in whole or in part to clients or third persons that are in the lawyer's possession in connection with a representation separate from the lawyer's own property. Funds shall be kept in a separate account, designated as a "trust" or "escrow" account, maintained in the state where the lawyer's office is situated, or elsewhere with the consent of the client or third person. Other client property shall be identified as such and appropriately safeguarded. Complete records of such account funds and other property shall be kept by the lawyer and shall be preserved for a period of [five years] after termination of the representation.

> (b) Upon receiving funds or other property in which a client or third person has an interest, a lawyer shall promptly notify the client or third person. Except as stated in this rule or otherwise permitted by law or by agreement with the client, a lawyer shall promptly deliver to the client or third person any funds or other property that the client or third person is entitled to receive and, upon request by the client or third person, shall promptly render a full accounting regarding such property.

Tex. Disciplinary R. Prof. Conduct 1.14, *reprinted in* Tex. Gov't Code Ann., tit 2, subtit. G app. A (Vernon's Supp.1998) (Tex. State Bar R. Art. X, § 9). The Comment to this Rule reads:

> A lawyer should hold property of others with the care required of a professional fiduciary. . . . All property which is the property of clients or third persons should be kept separate from the lawyer's business and personal property and, if monies, in one or more trust accounts. . . .
>
> The obligations of a lawyer under this Rule are independent of those arising from activity other than rendering legal services. For example, a lawyer who serves as an escrow agent is governed by the applicable law relating to fiduciaries even though the lawyer does not render legal services in the transaction.

*Id.* The Court finds that allowing attorneys to benefit from their clients' trust accounts, even if they pass this benefit on to clients, would qualify as an ethical violation. Therefore, the Court must discount Plaintiffs' argument regarding net benefit.

More importantly, the Court finds that Plaintiffs' arguments about "net benefit" and theoretical costs are made somewhat in a vacuum. Plaintiff's have failed to present any evidence that Mr. Summers' money, either the $1000 or the $250, did and could generate net benefit or net interest if not for IOLTA. Plaintiffs failed to establish an actual number denominating Mr. Summers' loss. With regard to *this case* and *Mr. Summers'* monies, Plaintiffs have failed to carry their burden of proof. Although this case turns on endless abstractions and near impossible mathematical conclusions it is without doubt that at a minimum Plaintiffs must present evidence to this Court that Mr. Summers is materially worse off because of IOLTA. At trial Mr. Summers testified that he is no worse off because of IOLTA. Transcript at 136.

The main source of net interest derived from IOLTA is generated by corporate and partnership monies which are disallowed from earning interest by federal banking law. Mr. Summers' money, since this Court has determined that it indeed belongs to him, is not the type of money from which IOLTA derives a great benefit. In fact, it is entirely possible, that Mr. Summers' money, placed in an IOLTA account, derived a negative benefit to IOLTA. *See* Testimony of Frank Newton at Transcript 225 (stating that 46-47% of IOLTA accounts cause TEAJF to lose money and that TEAJF pays negative fees). Plaintiffs fail to challenge 12 U.S.C. § 1832(a) and 12 C.F.R. § 204.130 (1997), which without a doubt, make possible and provide the greatest source of income for IOLTA.

The Court finds, based upon the evidence before the Court regarding in-firm pooling and sub-accounting, that without IOLTA the interest generated by Mr. Summers' principal would possess no economically realizable value. Plaintiffs have failed to present evidence of a loss. The Court finds that, based upon all the evidence before it, Mr. Summers's loss is zero. The Court finds that with regard to

the Plaintiffs' net benefit theory, Plaintiff's loss is also nothing. Even if the Court accepted Plaintiffs' theory, Plaintiffs failed to establish how and in what amount this "net benefit" would be passed on to clients. Without an identifiable compensable loss, the Court finds there has been no taking without compensation in violation of the Fifth Amendment.[8] Accordingly Plaintiffs' Fifth Amendment claims fail. However, as directed by the Supreme Court and the Fifth Circuit Court of Appeals, this Court will go on to address the related issue of whether a taking has occurred.

*B. Has a Taking Occurred?*

*1. Per Se Analysis v. Ad Hoc Analysis*

The United States Supreme Court has distinguished two general categories of takings: per se takings and regulatory takings. Government action that deprives property owners of all productive use of their property or physically invades property boundaries is often determined to be a per se or categorical taking. *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982). If a government regulation is not considered a per se taking, this Court must still consider whether a regulatory taking has occurred by considering three different factors: 1) the severity of the economic impact on the takings claimant; 2) the extent to which the regulation interferes with investment-backed expectations; and 3) the character and benefits of the government regulation. *Penn Central Transportation Co. v. City of New York*, 438 U.S. 104, 98

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[8] Although the Plaintiffs are only requesting declaratory and injunctive relief, they must still prove that a taking occurred "without just compensation" in order to establish a violation of the Fifth Amendment, which is a prerequisite to relief. *First English Evangelical Lutheran Church of Glendale v. County of Los Angeles*, 482 U.S. 304, 314- 315, 107 S.Ct. 2378, 96 L.Ed.2d 250 (1987).

S.Ct. 2646, 57 L.Ed.2d 631 (1978). The panel's opinion in the instant case gave no explicit indication whether the court viewed the case as a regulatory or per se takings case. *Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 106 F.3d 640, 645 (5th Cir.1997) (Benavides, J., dissenting from decision to failure to grant rehearing en banc). Thus, this Court must determine whether to apply a per se or regulatory analysis with limited guidance from the higher courts.

Plaintiffs argue that a per se takings analysis is applicable when the government invades or appropriates private property. *Loretto v. Teleprompter Manhattan CATV Corp.,* 458 U.S. 419, 427, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982); *Lucas v. South Carolina Coastal Council,* 505 U.S. 1003, 112 S.Ct. 2886, 120 L.Ed.2d 798 (1992); *Kaiser Aetna v. United States,* 444 U.S. 164, 100 S.Ct. 383, 62 L.Ed.2d 332 (1979). Plaintiffs further maintain that a per se analysis is appropriate when, as in this case, the property in issue is money. *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980). Plaintiffs also assert a related argument that a per se taking has occurred because Plaintiff has lost the right to exclude others from making beneficial use of his property.

Defendants maintain that per se analysis is inappropriate in this case and that the "ad hoc, factual" takings inquiry set forth in *Penn Central Transportation Co. v. City of New York,* 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978), should apply. Defendants assert that *Loretto* and *Kaiser Aetna* relate to the permanent physical invasion of real property. They further argue that appropriation of money does not qualify as a physical appropriation of property since money is fungible, "unlike real or personal property." *United States v. Sperry,* 493 U.S. 52, 62 n. 9, 110 S.Ct. 387, 107 L.Ed.2d 290 (1989).

Defendants further contend that the Supreme Court did not apply a per se takings analysis in *Webb's Fabulous Pharmacies* and that the balancing of interests in that case was inconsistent with a per se takings analysis. Defendants argue that the takings claims succeeded in *Webb's* not because the Court applied a per se test, but because the state offered no reasonable basis to support the monetary analysis.

The Court finds that Defendants are correct and that *Loretto, Lucas,* and *Kaiser Aetna* all differ from this case because those cases involve the physical invasion of real property. The Court finds that Plaintiff's related right to exclusion claim fails because the cases he relies on for that proposition all deal with real property, and this case deals with money, which is fungible. *Sperry,* at 62 n. 9, 110 S.Ct. 387. Therefore, Plaintiffs cannot rely on the real property cases to establish that a per se analysis is applicable here. However, Plaintiffs assert that this differentiation between cases where a per se analysis is applied from those in which an ad hoc analysis is applied, fails to explain the Supreme Court's holding in *Webb's Fabulous Pharmacies.*[9] Plaintiffs assert that Webb's did not involve real property and yet the Court applied a per se analysis. This Court begins with analysis of *Webb's,* since the Supreme Court relied on that case in determining that Plaintiffs possess a property interest in the interest generated by funds placed in IOLTA accounts. *Phillips v. Washington Legal Foundation,* 524 U.S. 156, 118 S.Ct. 1925, 1934, 141 L.Ed.2d 174 (1998).

In *Webb's,* the Supreme Court found that a Florida statute, allowing a Florida county to take the interest generated by an interpleader fund as its own, when that county charged a separate fee for the clerk's services in

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[9] *Webb's* was decided before the Supreme Court articulated the per se test.

receiving the fund into the registry, was violative of the Fifth Amendment. *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 156, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980). The appellant in that case filed an interpleader action in Florida state court and tendered the sum at issue, nearly $2 million, to the court. In addition to deducting $9,228.74 from the interpleader fund as a fee "for services rendered," the clerk of court also retained the more than $100,000 in interest income generated by the deposited funds. *Id.* at 157, 101 S.Ct. 446. The Supreme Court held that the statute authorizing the clerk to confiscate the earned interest violated the Takings Clause. *Id.* at 164, 101 S.Ct. 446. The Supreme Court stated, "a State by *ipse dixit*, may not transform private property into public property without compensation" simply by legislatively abrogating the traditional rule that "earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property." *Id.* The Court distinguished "confiscatory regulations" from "those regulating the use of property" and stated that "a State may not sidestep the Takings Clause by disavowing traditional property interests long recognized under state law." *See id.,* at 163-164, 101 S.Ct. 446; *see also Lucas v. South Carolina Coastal Council,* 505 U.S. 1003, 1029, 112 S.Ct. 2886, 120 L.Ed.2d 798 (1992).

In this case, the Court finds IOLTA does not qualify as a confiscatory regulation of Mr. Summers' property. Distinguishable from *Webb's,* the instant case is one where the client's money cannot be placed in an IOLTA fund unless it cannot earn interest elsewhere. Tx. R. Equal Access Rule 4B, 6 (West 1999). In *Webb's,* there was net interest in issue. *Webb's* at 163, 101 S.Ct. 446. Net interest could have been earned on that money regardless of whether it was interpleaded into the court or held in a private bank account. In this case the legislative and regulatory framework makes net interest impossible outside of the context of IOLTA; but for IOLTA, the money necessarily would lie fallow.

The monetary interest at issue in *Webb's* arose out of the operation of a specific, separately identifiable fund of money, from which the government collected a fee. *See Eastern v. Apfel,* 524 U.S. 498, 118 S.Ct. 2131, 2134, 141 L.Ed.2d 451 (1998). In *Webb's* net interest was extant even after the applicable fees were subtracted from the principal. In this case, the costs of generating interest exceed the interest a client could earn, or by definition the funds would not be placed in IOLTA. On this basis the instant case is easily distinguishable from *Webb's.* In the instant case there is no money to confiscate outside the mechanisms which make IOLTA possible, therefore it cannot qualify as a confiscatory taking.[10] *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980).

The Supreme Court stated in *Phillips,* "[a]s to the principal, then the IOLTA rules at most 'regulate the use of the property'" *Phillips,* 118 S.Ct. at 1930 (citing *Yee v. City of Escondido,* 503 U.S. 519, 522, 112 S.Ct. 1522, 118 L.Ed.2d 153 (1992)). The Court finds that this case is one in which the interference with property cannot be characterized as a physical invasion by the government. Plaintiffs claimed interference clearly stems from "some program adjusting the benefits and burdens of economic life to promote the common good." *Penn Central,* 438 U.S. at 116-118, 98 S.Ct.

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[10] The test the Court applied in *Webb's,* arguably the case most on point with the instant case, seems to fall somewhere in between a per se and regulatory ad hoc analysis. Plaintiffs seemingly acknowledge this and offer a new, three-prong test for this Court to apply. The Court declines to do so. The articulation of a new test in the area of takings law is a task better left to a higher Court. However, the Court could find that even applying a hybrid test Plaintiff's claims would fail. The exaction in this case does not go to general government revenues, but is earmarked to legal services and this cost is reasonably related to the costs of using a lawyer.

2646. Therefore, the Court finds that the ad hoc analysis consistent with a claims of a regulatory taking is applicable.

Government regulation often "curtails some potential for the use or economic exploitation of private property," *Andrus v. Allard,* 444 U.S. 51, 65, 100 S.Ct. 318, 62 L.Ed.2d 210 (1979), and "not every destruction or injury to property by governmental action has been held to be a 'taking' in the constitutional sense," *Armstrong v. United States,* 364 U.S. 40, 48, 80 S.Ct. 1563, 4 L.Ed.2d 1554 (1960). "In light of that understanding, the process for evaluating a regulation's constitutionality involves an examination of the "justice and fairness" of the governmental action." *Eastern Enterprises v. Apfel,* 118 S.Ct. at 2146. "That inquiry, by its nature, does not lend itself to any set formula." *Id.* The determination is essentially ad hoc and fact intensive. *Kaiser Aetna v. United States,* 444 U.S. 164, 175, 100 S.Ct. 383, 62 L.Ed.2d 332 (1979). The Supreme Court has identified several factors that have particular significance: "the economic impact of the regulation, its interference with reasonable investment backed expectations, and the character of the governmental action." *Penn Central,* 438 U.S. at 124, 98 S.Ct. 2646.

*2. Applying the Ad Hoc Analysis*

The Court now considers: 1) the economic impact of the regulation; 2) the extent of interference with "distinct investment backed expectations"; and 3) the nature of the governmental action. *Penn Central Transportation Co. v. City of New York,* 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978).

Defendants argue that at most, the Texas IOLTA Program has no impact on the client principal or interest. Defendants argue that since the client could not have earned net interest absent IOLTA, there is no economic impact on the client, Mr. Summers. Plaintiffs assert that the economic impact factor tips in their favor, because IOLTA expropriates 100% of the interest earned on IOLTA. The Court finds that

the costs of administering the money placed in a non-IOLTA account exceed those in an IOLTA account. These costs would subsume the interest earned if not for IOLTA. The client's funds would be unable to generate net interest absent IOLTA. Therefore the economic impact of the regulation on Plaintiffs is nill. Moreover, in the absence of IOLTA, the money would necessarily generate no interest for anyone but the banks. *See* 12 U.S.C. § 1832(a); *see also* Tex. Disciplinary R. Prof. Conduct 1.14(b), *reprinted in* Tex. Gov't Code Ann., tit 2, subtit. G app. A (Vernon's Supp.1998) (Tex. State Bar R. Art. X, § 9).

Defendants further argue that Plaintiffs have no reasonable, investment-backed expectation in the interest earned on principal placed in IOLTA. This is because, Defendants argue, if the Plaintiffs' funds could earn interest outside of IOLTA the funds should not be placed in IOLTA. Therefore any expectation of interest could only be created by IOLTA itself and would disappear without IOLTA. However, Plaintiffs note in *Webb's* that the Court found a compensable taking had occurred despite the fact that the parties in that case had no right to insist that the court holding the interpleaded funds invest the money. The Court found that, once the funds were invested, the owner of the principal owned the interest. Once again, this Court distinguishes *Webb's* based on the fact that net interest was in issue that could have been earned regardless of whether the funds were held by the court or by the owner. In this case, Plaintiffs cannot hold a legitimate investment-backed expectation of interest when funds placed in IOLTA cannot by definition earn net interest.

Defendants further assert that IOLTA is a beneficial government program which by regulation transfers the benefit (the "use value") of funds unable to earn interest outside of IOLTA from banks to TEAJF in order to provide legal services to the poor. Plaintiffs respond that the

character of the government action, in this case the expropriation of money, suggest that the IOLTA program constitutes a compensable taking. Plaintiffs argue that they have been unfairly singled out by the government to bear a burden they had no role in creating. *Eastern Enterprises v. Apfel,* 524 U.S. at 520, 118 S.Ct. 2131.

Plaintiffs in the instant action cannot maintain they are being unfairly singled out to bear a burden, when they are in fact bearing no burden at all. The IOLTA program costs Plaintiffs nothing. The governmental action in this case does not implicate fundamental principles of "justice and fairness" because there is no cost to Plaintiffs. *Id.*

Employing an ad hoc analysis, and applying the fundamental principles of justice and fairness the Court finds that a taking has not occurred. The IOLTA Program is not in any way unfair to Plaintiffs. "It cannot be said that the Takings Clause is violated whenever legislation requires one person to use his or her assets for the benefit of another." *Connolly v. Pension Benefit Guar. Corp.,* 475 U.S. 211, 223, 106 S.Ct. 1018, 89 L.Ed.2d 166 (1986). Therefore, Plaintiffs' Fifth Amendment claims fail on this additional basis.

**IT IS THEREFORE ORDERED, ADJUDGED AND DECREED** that all Plaintiffs' claims against all Defendants in this cause of action are hereby **DISMISSED WITH PREJUDICE.**

**IT IS FURTHER ORDERED** that this cause of action is **CLOSED** and that all pending motions are hereby **DENIED AS MOOT.**

UNITED STATES DISTRICT COURT, W.D. TEXAS, AUSTIN DIVISION.

WASHINGTON LEGAL FOUNDATION, et al.,
v.
TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION, et al.
No. A-94-CA-081 JN.

Jan. 4, 2000.

NOWLIN, District Judge.

Before the Court are: the Justices of the Texas Supreme Court's Motion for Judgment on the Pleadings (Clerk's Doc. No. 78); Plaintiffs' Response to the Supreme Court Justices' Motion for Judgment on the Pleadings (Clerk's Doc. No. 98); and, Reply of the Justices of the Texas Supreme Court to Plaintiffs' Response to Motion for Judgment on the Pleadings (Clerk's Doc. No. 102).

*I. Background*

The Plaintiffs in this cause of action are: the Washington Legal Foundation, a non-profit public interest law and policy center; Michael Mazzone, a Texas resident and attorney licensed to practice law by the State Bar of Texas; and William Summers, a Texas resident and consumer of legal services. Plaintiffs bring this case pursuant to 42 U.S.C. § 1983 asserting that Defendants' mandatory Interest on Lawyers' Trust Account ("IOLTA") program violates the First and Fifth Amendments of the United States Constitution. The IOLTA program is implemented and overseen by Defendant the Texas Equal Access to Justice Foundation ("TEAJF"). In 1984,

Defendants the Texas Supreme Court Justices adopted Article XI of the Rules of the State Bar of Texas which established the IOLTA program.

By Order dated January 19, 1995, this district court granted summary judgment for the Defendants on the basis that the Plaintiffs could not establish a constitutionally cognizable property interest because, but for the IOLTA program, no interest could be earned on the funds in the IOLTA account. *Washington Legal Foundation v. Texas Equal Access to Justice Foundation*, 873 F.Supp. 1, 7 (W.D.Tex.1995). The Fifth Circuit reversed this court, concluding that the interest earned on client funds held in IOLTA accounts is a property interest within the reach of the Fifth Amendment. *Washington Legal Foundation v. Texas Equal Access to Justice Foundation*, 94 F.3d 996 (5th Cir.1996). The Supreme Court affirmed the Fifth Circuit's decision and determined that clients have a "property interest" in the interest income generated by the Texas IOLTA program. *Phillips v. Washington Legal Foundation*, 524 U.S. 156, 118 S.Ct. 1925, 1934, 141 L.Ed.2d 174 (1998). This holding was limited to its determination of the existence of a property interest in the interest income. *Id.* The Supreme Court remanded the case for consideration of whether or not IOLTA funds have been "taken" by the State, as well as the amount, if any, of just compensation due the Plaintiffs. Thus this Court must once again consider the fate of IOLTA. Before the Court may address that issue, the Court must first consider whether the Texas Supreme Court Justice Defendants are immune from suit as they posit in their Motion for Judgment on the Pleadings. In their Motion for Judgment on the Pleadings, the Justices argue that: (a) they are immune from monetary damages asserted against them in their official capacities; (b) they possess legislative immunity for actions taken in a legislative capacity; and (c)

that injunctive relief requested by plaintiffs is not yet ripe, and in any event, is also barred by legislative immunity.

*II. Motion for Judgment on the Pleadings*

A motion brought pursuant to Fed.R.Civ.P. 12(c) is designed to dispose of cases where the material facts are not in dispute and a judgment on the merits can be rendered by looking to the substance of the pleadings and any judicially noticed facts. 5A Wright & Miller, Federal Practice & Procedure, § 1367 at 509-10 (1990); *see J.M. Blythe Motor Lines Corp. v. Blalock*, 310 F.2d 77, 78-79 (5th Cir.1962). The facts of the instant case are not in dispute. A motion brought under Fed.R.Civ.P. 12(c) is specifically designed to facilitate this inquiry. 5A Charles A. Wright & Arthur R. Miller, Federal Practice & Procedure, § 1367 at 511 ("The motion for a judgment on the pleadings only has utility when all material allegations of fact are admitted in the pleadings and only questions of law remain.").

Rule 12(c) motions may be filed after the pleadings are closed. Such motions will be treated as a motion for judgment on the pleadings based on a failure to state a claim on which relief may be granted. *See National Ass'n of Pharmaceutical Mfrs. v. Ayerst Laboratories*, 850 F.2d 904, 909 n. 4 (2d Cir.1988).

*III. Monetary Damages*

The named Defendant Texas Supreme Court Justices assert that they are absolutely immune from suit and should be dismissed from this cause of action. First, they assert that they possess official capacity immunity from monetary damages. *Will v. Michigan Dep't of State Police*, 491 U.S. 58, 109 S.Ct. 2304, 105 L.Ed.2d 45 (1989). The Plaintiffs agree and assert that there are no claims for monetary

damages extant against the Supreme Court Justices. In light of this, the Court grants Defendants' Motion for Judgment on the Pleadings with regard to all claims against them for monetary damages.

*IV. The Justices' Claims of Legislative Immunity*

Plaintiffs however, continue to claim that they are entitled to injunctive relief against the Supreme Court Justice Defendants. Along with their request for declaratory relief that this Court find the IOLTA program unconstitutional, Plaintiffs request that this Court enjoin the currently sitting Texas Supreme Court Justices from "adopting any rules that purport to require attorneys, as a condition for practicing law in Texas, to handle client trust account funds in a manner designed to ensure that interest on those funds will accrue to anyone not designated by the client." *See* Plaintiffs' Complaint at 15. Plaintiffs further seek to enjoin the Justices from imposing disciplinary sanctions on attorneys who fail to comply with the IOLTA rules. *Id.*

The Texas Supreme Court Defendants claim that they are absolutely immune from suit for injunctive relief because in adopting the IOLTA rules they were acting in a legislative capacity. *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719, 731-34, 100 S.Ct. 1967, 64 L.Ed.2d 641 (1980). Plaintiffs agree that the Justices of the Court enjoy absolute immunity for their legislative acts in adopting IOLTA. Plaintiffs assert that their claims against the Texas Supreme Court Justices are not brought against them in their legislative capacity, but in capacity of the Texas Supreme Court Justices' ability to enforce the IOLTA rules. *Id.*; *Snoeck v. Brussa*, 153 F.3d 984 (9th Cir.1998). Plaintiffs assert that the Supreme Court of Texas is a proper defendant in an action to enjoin it from "taking disciplinary action against any attorney for failing to

place client trust funds into an IOLTA account." *See* Complaint at 15.

*A. Legislative Immunity*

Legislative immunity is derived from the "speech and debate clause" found in the United States Constitution. U.S. Const. art. I, § 6; *see also Tenney v. Brandhove*, 341 U.S. 367, 372-73, 71 S.Ct. 783, 95 L.Ed. 1019 (1951). The Supreme Court has determined that the Speech or Debate Clause immunizes Congressmen from suits for either prospective relief or damages. *Eastland v. United States Servicemen's Fund*, 421 U.S. 491, 502-503, 95 S.Ct. 1813, 44 L.Ed.2d 324 (1975). The purpose of this immunity[11] is to insure that the legislative function may be performed independently without fear of outside interference. *Ibid.* To preserve legislative independence, the Supreme Court

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[11] Legislative immunity is a different concept from Eleventh Amendment immunity. The Eleventh Amendment prohibits the federal courts from entertaining "any suit in law or equity, commenced or prosecuted against one of the United States by Citizens of another State, or by Citizens or Subjects of any Foreign State." U.S. Const. Amend. XI. The bar imposed by the Eleventh Amendment has been extended, by judicial construction, to suits brought against states by their own citizens. *See Hans v. Louisiana*, 134 U.S. 1, 10 S.Ct. 504, 33 L.Ed. 842 (1890); *see also Edelman v. Jordan*, 415 U.S. 651, 662, 94 S.Ct. 1347, 39 L.Ed.2d 662 (1974). The Eleventh Amendment bars suits brought directly against a state, absent the state's consent, irrespective of the nature of the relief sought. *See Hutto v. Finney*, 437 U.S. 678, 700, 98 S.Ct. 2565, 57 L.Ed.2d 522 (1978); *see also Alabama v. Pugh*, 438 U.S. 781, 98 S.Ct. 3057, 57 L.Ed.2d 1114 (1978). The Eleventh Amendment does not, however, bar suits seeking declaratory or injunctive relief against state officers. *See Ex Parte Young*, 209 U.S. 123, 28 S.Ct. 441, 52 L.Ed. 714 (1908). The Eleventh Amendment is jurisdictional in the sense that it limits the federal court's power, and therefore can be raised at any stage in the proceedings. *Calderon v. Ashmus*, 523 U.S. 740, 118 S.Ct. 1694, 140 L.Ed.2d 970 (1998).

determined that "legislators engaged 'in the sphere of legitimate legislative activity,' *Tenney v. Brandhove* [341 U.S. 367, 376, 71 S.Ct. 783, 95 L.Ed. 1019 (1951)], should be protected not only from the consequences of litigation's results but also from the burden of defending themselves." *Dombrowski v. Eastland*, 387 U.S. 82, 85, 87 S.Ct. 1425, 18 L.Ed.2d 577 (1967). Individuals who are not legislators, but who are acting in a capacity comparable to that of a legislator, are also entitled to the immunity. *Hughes v. Lipscher*, 852 F.Supp. 293, 298 (D.N.J.1994). Not all actions taken by officials with legislative duties, however, are protected by legislative immunity. *Hughes v. Tarrant County*, 948 F.2d 918, 920 (5th Cir.1991). Legislative immunity protects only those duties that are functionally legislative. *Id.* Although there is no absolute standard by which to distinguish between legislative and nonlegislative acts, courts have consistently recognized a distinction between the legislative act of establishing a policy, act, or law and the nonlegislative act of enforcing or administering that policy, act, or law. *See Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719, 731-34, 100 S.Ct. 1967, 64 L.Ed.2d 641 (1980).

*B. Supreme Court of Virginia*

*Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719, 731-34, 100 S.Ct. 1967, 64 L.Ed.2d 641 (1980), holds that in the instance of a court promulgating a rule, in that case the Virginia Code of Professional Responsibility, a court acts in its legislative capacity and is therefore immune from suit. However, the Supreme Court goes on to say that, because the Virginia Court possessed independent enforcement power "beyond that of merely adjudicating complaints filed by others and beyond the normal authority of the courts to punish attorneys for contempt," the Virginia Court was not shielded by

immunity in its enforcement capacity. *Id.* The Court's decision hinged on the fact that various sections of the Virginia Code of Professional Responsibility empowered the Virginia Court with "independent power of its own to initiate proceedings against attorneys." *Id.* at 736, 100 S.Ct. 1967. Thus this Court's decision regarding the immunity of the Supreme Court Justices depends at least in part on whether the Court finds that the Justices have the independent authority to enforce the IOLTA rules.

*C. Independent Authority to Enforce IOLTA*

Plaintiffs argue that the Supreme Court of the State of Texas retains the independent power to enforce the IOLTA rules for immunity purposes. First, Plaintiffs cite to the Preamble to the Texas Rules of Disciplinary Procedure:

> The Supreme Court of Texas has the constitutional and statutory responsibility within the State for lawyer discipline and disability system, and has inherent power to maintain appropriate standards of professional conduct and to dispose of individual cases of lawyer discipline.

*See* TEX. GOV'T CODE ANN., tit. 2, subtit. G, App A-1 (Vernon 1998). According to the Plaintiffs, the Supreme Court Justices maintain the independent authority to enforce the IOLTA rules, and that for this reason they are appropriate defendants. Although this argument is not without merit, it is ultimately unpersuasive. In Supreme Court of Virginia, the United States Supreme Court's decision that the Virginia Court was not immune was not based only upon its "inherent power to discipline attorneys;" but rather upon the fact that "[the Virginia statute in issue] expressly provides that if the Virginia Court or any other court of record observes any act

of unprofessional conduct, it may itself, without any complaint being filed by the State Bar or by any other third party, issue a rule to show cause against the offending attorney." *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719, 724, 100 S.Ct. 1967, 64 L.Ed.2d 641 (1980). In the instant case TEAJF and the State Bar play an integral part in the pursuit of attorney compliance with IOLTA. It is these entities that initiate all noncompliance proceedings. *See* Rules Governing the Operation of the Texas Equal Access to Justice Foundation, Rule 24 (West's Rules of Court 1999). Moreover, the Preamble cited by Plaintiff goes on to state that "the responsibility for administering and supervising lawyer discipline and disability is delegated to the Board of Directors to the State Bar of Texas." *See* TEX. GOV'T CODE ANN., tit. 2, subtit. G, App A-1 (Vernon 1998). The Court finds that based upon this Plaintiffs' argument is devoid of merit.

*D. Rule 24*

Rule 24[12] of the Rules Governing the Operation of the Texas Equal Access to Justice Foundation delineates the

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[12] RULE 24. COMPLIANCE

(a) On or after June 1 of each year, all attorneys licensed by the Supreme Court of Texas shall report IOLTA compliance in a manner to be prescribed by the Texas Equal Access to Justice Foundation and the State Bar of Texas. Such compliance statements may require such information as is deemed reasonably necessary by the Foundation and the State Bar of Texas and shall be signed by the reporting attorney.

(b) Each attorney must complete an annual compliance statement and return it to the Foundation by the date stated on the compliance statement. If the compliance statement is timely filed, indicating compliance, there will be no acknowledgement. The presumption of compliance after timely filing shall obtain, absent some evidence to the contrary.

(continued...)

procedure an attorney must follow to be compliant with IOLTA. *See*Rules Governing the Operation of the Texas Equal Access to Justice Foundation, Rule 24 (West's Rules of Court 1999). Plaintiffs argue that the language of Rule 24 makes it clear that the Supreme Court retains the ability to discipline attorneys directly.

Defendants respond that Rule 24 provides no role for the Justices of the Supreme Court in the process of disciplining lawyers for failure to comply with IOLTA. Defendants assert that the Supreme Court cannot independently take action under Rule 24; it can only take action if the Texas Equal Access to Justice Foundation and State Bar take action, which they are capable of doing without any involvement from the Supreme Court of Texas.

Plaintiffs rely on the language in 24(d)(ii) "the attorney shall be immediately suspended as an attorney licensed to practice law in the State of Texas until a compliance statement is filed" as stating that the Supreme Court Justices retain the independent authority to suspend

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(footnote continued)

(c) Should a compliance statement filed by an attorney fail to evidence compliance, the Foundation shall contact the attorney and attempt to resolve administratively the non-compliance.

(d) The Foundation shall furnish annually to the State Bar of Texas a list of all attorneys licensed by The Supreme Court of Texas (i) who have not timely filed a compliance statement or (ii) as to whom the Foundation has been unable administratively to resolve any impediment to the proper filing of a compliance statement. The State Bar of Texas shall send to each person so reported, by certified mail, return receipt requested, a non-compliance notice. Should the attorney fail or refuse to file the compliance statement within thirty (30) days of such notice, the State Bar of Texas shall so notify the Clerk of The Supreme Court of Texas, and the attorney shall be immediately suspended as an attorney licensed to practice law in the State of Texas until a compliance statement is filed.

attorneys. Plaintiffs argue that because Rule 24 mandates automatic suspension of any attorney who fails to comply, and does not specifically state that the State Bar or some other entity should suspend the noncompliant attorney, the Court has not delegated this power.

The Court finds it difficult to follow Plaintiffs' reasoning. The Court finds that reading Rule 24, it is apparent that after being notified by the State Bar and at the behest of the State Bar, the Clerk of the Supreme Court of Texas is the individual responsible for suspending noncompliant attorneys. Although the Rule does not directly specify in the clause in issue a subordinate body to perform the ministerial act of suspension, it is clear that the Supreme Court Justices do not themselves perform this act. When read in its entirety, it is evident that after the State Bar notifies the Clerk of the Supreme Court of a lawyer's failure to provide a compliance statement, the Clerk of the Supreme Court is charged with taking action. The Justices themselves are not referred to in the chain of noncompliance. Therefore, the Justices do not have the independent power to enforce Rule 24.

*E. Rule 24, Read Along With Rule 25*

Plaintiffs further argue that when read along with Rule 25,[13] which Plaintiffs allege provides that the Supreme

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[13] RULE 25. REVIEW AND APPEAL

(a) An attorney may file a written request based upon good cause for exemption from compliance with any of the requirements of these Rules, an extension of time for compliance, an extension of time to comply with a deficiency notice, or an extension of time to file an annual compliance statement. Such request shall be reviewed and determined by a Committee established by the State Bar or by such committee as the

(continued...)

Court is the final arbiter regarding whether an attorney is entitled to an exemption, Rule 24 provides the Justices with independent enforcement power of IOLTA. Defendants assert that this reading is erroneous. Defendants assert that the Texas Supreme Court has no independent enforcement power of this rule. Defendants assert that Supreme Court of Virginia holds that the ability to initiate disciplinary actions deprives the Justices of immunity. Defendants argue that in this case the Supreme Court Justices do not have that ability. This Court agrees.

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(footnote continued)

chairperson may, from time to time, designate. The attorney shall be promptly notified of the decision by the Committee.

(b) "Good cause" shall exist when an attorney is unable to comply with this Article because of extraordinary hardship or extenuating circumstances which were not willful on the part of the attorney and were beyond his or her control.

(c) Should the decision of the Committee be adverse to the attorney, the attorney may request the Board of Directors of the State Bar to review the decision by making such request in writing to the Executive Director of the State Bar within thirty days of notification of the decision of the Committee. The Chairman of the Board may appoint a committee of the Board to review the decision of the Committee and make a recommendation to the Board. The decision shall be made by the Board.

(d) Should the decision of the Board be adverse to the attorney, the attorney may appeal such decision by filing suit within thirty days of notification of the Board's action, failing which the decision of the Board shall be final. Such suit shall be brought against the State Bar, and shall be filed in a district court in Travis County, Texas. Trial shall be de novo, but the burden of proof shall be on the attorney appealing, the burden shall be by a preponderance of the evidence, and the attorney shall prove the existence of "good cause" as defined herein. The trial court shall proceed to hear and determine the issue without a jury. Either party shall have a right to appeal.

(e) Any suspension of an attorney shall be vacated during the administrative review process and while any suit filed is pending.

Moreover, Defendants argue that Plaintiffs reading of Rules 24 and 25 is incorrect. Defendants assert that Plaintiffs are attempting to apply Rule 25 even though it has no relationship to the facts of this case. Rule 25 provides for judicial review of adverse decisions of the Board of Directors of the State Bar when an attorney requests exemption from the IOLTA program, an extension of time to comply, an extension of time to comply with a deficiency notice or an extension of time to file a compliance statement. This rule has no relation to Rule 24 and its command that attorneys who fail to file a compliance statement should be suspended as an attorney licensed to practice in the State of Texas. Therefore these two rules cannot be read in conjunction in order to create an independent enforcement power on behalf of the Supreme Court Justices.

Plaintiffs further rely on a Ninth Circuit case, *Snoeck v. Brussa*, 153 F.3d 984 (9th Cir.1998), in support of their claims. In that case the Ninth Circuit found that the only proper defendant for a challenge to a rule promulgated by the Nevada Commission on Judicial Discipline was the Nevada Supreme Court. This decision was based upon the fact that the Nevada Supreme Court had the sole authority to enforce the rule by holding violators in contempt of court. Plaintiffs assert that since the Justices adopted Rule 24(d), which provides for the automatic suspension of attorneys who fail to comply with the compliance statement requirements, they have not ceded their independent enforcement power of the IOLTA rules.

First the Court notes that *Snoeck* is a Ninth Circuit case and thus has no precedential value in this Circuit. The Court further finds that *Snoeck* is distinguishable from the instant case and from Supreme Court of Virginia. *Snoeck* deals with Eleventh Amendment immunity and not legislative immunity unlike the instant case and Supreme

Court of Virginia. Also, the Court finds that the dissent in that case is instructive in its argument that the members of the Nevada Commission on Judicial Discipline were in fact the proper defendants and not the Supreme Court of Nevada:

> In all of these cases, the named officers could, at most, initiate proceedings to enforce the challenged statute--which is exactly what the Commission does. Those officers had no power to hold wrongdoers in contempt or other wise to impose any punishment. That, to repeat, is the function of the courts. Thus, it is irrelevant that the Commission, like all prosecutorial authorities, cannot actually impose punishment.

*Snoeck*, 153 F.3d at 990.

The Court finds that the independent power to enforce IOLTA does not in fact lie with the Justices of the Supreme Court of Texas and that therefore they are immune pursuant to *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719, 731-34, 100 S.Ct. 1967, 64 L.Ed.2d 641 (1980). The Court finds the Justices of the Supreme Court of Texas are entitled to legislative immunity in the face of Plaintiffs' claims against them. The Texas Supreme Court Justices, unlike those in Supreme Court of Virginia, do not possess the independent power to initiate disciplinary actions against attorneys. Since the Texas Supreme Court Justice Defendants do not possess independent enforcement powers the Court finds they are absolutely immune pursuant to Supreme Court of Virginia.

*V. Case or Controversy*

Since the Court has found that the Justices possess legislative immunity, it is unnecessary to address their assertions regarding whether or not this case presents a justiciable case or controversy pursuant to Article III of the Constitution.

*VI. Order*

**IT IS THEREFORE ORDERED, ADJUDGED AND DECREED** that the Supreme Court Justices' Motion for Judgment on the Pleadings (Clerk's Doc. No. 78) is hereby **GRANTED**.

**IT IS FURTHER ORDERED** that all of Plaintiffs' claims against the named Supreme Court Defendants, Defendants Thomas R. Phillips, Raul Gonzales, Jack Hightower, Nathan L. Hecht, Lloyd A. Doggett, Bob Gammage, Craig Enoch, John Cornyn, Rose Spector, and the individuals currently serving on the Texas Supreme Court are hereby **DISMISSED**.

SUPREME COURT OF THE UNITED STATES

No. 96-1578

Thomas R. PHILLIPS, et al., Petitioners,

v.

WASHINGTON LEGAL FOUNDATION et al.

Argued January 13, 1998

Decided June 15, 1998

Chief Justice REHNQUIST delivered the opinion of the Court.

Texas, like 48 other States and the District of Columbia,[1] has adopted an Interest on Lawyers Trust

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[1] Ala. Rule Prof. Conduct 1.15(g) (1996); Alaska Rule Prof. Conduct 1.15(d) (1997); Ariz. Sup.Ct. Rule 44(c)(2) (1997); Ark. Rule Prof. Conduct 1.15(d)(2) (1997); Cal. Bus. & Prof.Code Ann. § 6211(a) (West 1990 and Supp.1998); Colo. Rule Prof. Conduct 1.15(e)(2) (1997); Conn. Rule Prof. Conduct 1.15(d) (1998); Del. Rule Prof. Conduct 1.15(h) (1998); D.C. Rule Prof. Conduct 1.15(e) (1997); Fla. Bar Rule 5-1.1 (1994 and Supp.1998); Ga.Code Prof. Responsibility Rule 3-109, DR 9-102 (1998); Haw. Sup.Ct. Rule 11 (1997); Idaho Rule Prof. Conduct 1.15(d) (1997); Ill. Rule Prof. Conduct 1.15(d) (1997); Iowa Code Prof. Responsibility DR 9-102 (1997); Kan. Rule Prof. Conduct 1.15(d)(3) (1997); Ky. Sup.Ct. Rule 3.830 (1998); La. Rule Prof. Conduct 1.15(d) (1997); Me. Code Prof. Responsibility 3.6(e)(4) (1997); Md. Bus. Occ. & Prof.Code Ann. § 10-303 (1995); Mass. Sup.Ct. Rule 3:07, DR 9-102 (1997); Mich. Rule Prof. Conduct 1.15(d) (1997); Minn. Rule Prof. Conduct 1.15(d) (1993); Miss. Rule Prof. Conduct 1.15(d) (1997); Mo. Rule Prof. Conduct 1.15(d) (1997); Mont. Rule Prof. Conduct 1.18(b) (1996); Neb. Sup.Ct. Trust AcCt. Rules 1-8 (1997); Nev. Sup.Ct. Rule

(continued...)

Account (IOLTA) program. Under these programs, certain client funds held by an attorney in connection with his practice of law are deposited in bank accounts. The interest income generated by the funds is paid to foundations that finance legal services for low-income individuals. The question presented by this case is whether interest earned on client funds held in IOLTA accounts is "private property" of either the client or the attorney for purposes of the Takings Clause of the Fifth Amendment. We hold that it is the property of the client.

I

In the course of their legal practice, attorneys are frequently required to hold client funds for various lengths of time. Before 1980, an attorney generally held such funds in noninterest-bearing, federally insured checking accounts in which all client trust funds of an individual attorney were pooled. These accounts provided administrative convenience

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(footnote continued)

217 (1998); Petition of New Hampshire Bar Assn., 122 N.H. 971, 453 A.2d 1258 (1982); N.J. Rules Gen. Application 1:28A-2 (1998); N.M. Rule Prof. Conduct 16-115(D) (1998); N.Y. Jud. Law § 497 (McKinney Supp.1997 and 1998); N.C. Rule Prof. Conduct 1.15-3 (1997); N.D. Rule Prof. Conduct 1.15(d)(1) (1997); Ohio Rev.Code Ann. § 4705.09(A)(1) (1997); Okla. Rule Prof. Conduct 1.15(d) (1997); Ore.Code Prof. Responsibility DR 9- 101(D)(2) (1997); Pa. Rule Prof. Conduct 1.15(d) (1997) and Pa. Rule Disciplinary Enforcement 601(d) (1997); R.I. Rule Prof. Conduct 1.15(d) (1997); S.C.App.Ct. Rule 412 (1988); S.D. Rule Prof. Conduct 1.15(d)(4) (1995); Tenn.Code Prof. Responsibility DR 9-102(C)(2) (1997); *In re Interest on Lawyers' Trust Accounts,* 672 P.2d 406 (Utah 1983); Va. Sup.Ct. Rules, Pt. 6, § 4, & para. 20 (1997); Vt.Code Prof. Responsibility DR 9-103 (1996); Wash. Rule Prof. Conduct 1.14(c)(1) (1997); W. Va. Rule Prof. Conduct 1.15(d) (1997); Wis. Sup.Ct. Rules 13.04, 20:1.15 (1997); Wyo. Rule Prof. Conduct 1.15(II) (1997). Indiana is the only State that has not implemented an IOLTA program. *See In re Indiana State Bar Association Petition,* 550 N.E.2d 311 (Ind.1990).

and ready access to funds. They were noninterest bearing because federal law prohibited federally insured banks and savings and loans from paying interest on checking accounts. *See* 12 U.S.C. § § 371a, 1464(b)(1)(B), 1828(g). When a lawyer held a large sum in trust for his client, such funds were generally placed in an interest-bearing savings account because the interest generated outweighed the inconvenience caused by the lack of check-writing capabilities.

In 1980, Congress authorized the creation of Negotiable Order of Withdrawal (NOW) accounts, which for the first time permitted federally insured banks to pay interest on demand deposits. § 303, 94 Stat. 146, as amended, 12 U.S.C. § 1832. NOW accounts are permitted only for deposits that "consist solely of funds in which the entire beneficial interest is held by one or more individuals or by an organization which is operated primarily for religious, philanthropic, charitable, educational, political, or other similar purposes and which is not operated for profit." § 1832(a)(2). For-profit corporations and partnerships are thus prohibited from earning interest on demand deposits. *See ibid.* However, interpreting § 1832(a), the Federal Reserve Board has concluded that corporate funds may be held in NOW accounts if the funds are held in trust pursuant to a program under which charitable organizations have "the exclusive right to the interest." Letter from Federal Reserve Board General Counsel Michael Bradfield to Donald Middlebrooks (OCt. 15, 1981), reprinted in Middlebrooks, The Interest on Trust Accounts Program: Mechanics of its Operation, 56 Fla. B.J. 115, 117 (Feb. 1982) (hereinafter Federal Reserve's IOLTA Letter).[2]

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[2] We express no opinion as to the reasonableness of this interpretation of § 1832(a). *See Chevron U.S.A. Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 844, 104 S.Ct. 2778, 2782- 2783, 81 L.Ed.2d 694 (1984).

Beginning with Florida in 1981, a number of States moved quickly to capitalize on this change in the banking regulations by establishing IOLTA programs. Texas followed suit in 1984. Its Supreme Court issued an order, now codified as Article XI of the State Bar Rules, providing that an attorney who receives client funds that are "nominal in amount or are reasonably anticipated to be held for a short period of time" must place such funds in a separate, interest-bearing NOW account (an IOLTA account). Tex. State Bar Rule, Art. XI, § 5(A); Rules 4, 7 of the Texas Rules Governing the Operation of the Texas Equal Access to Justice Program. Client funds are considered "nominal in amount" or "held for a short period of time" if the attorney holding the funds determines that

> "such funds, considered without regard to funds of other clients which may be held by the attorney, law firm or professional corporation, could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the account, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain the interest on such funds for the client." Texas IOLTA Rule 6.

Interest earned by the funds deposited in an IOLTA account is to be paid to the Texas Equal Access to Justice Foundation (TEAJF), a nonprofit corporation established by the Supreme Court of Texas. Tex. State Bar Rule, Art. XI, §§ 3, 4; Texas IOLTA Rule 9(a). TEAJF distributes the funds to nonprofit organizations that "have as a primary purpose the delivery of legal services to low income persons." Texas IOLTA Rule 10. The Internal Revenue Service does not attribute the interest generated by an IOLTA

account to the individual clients for federal income tax purposes so long as the client has no control over the decision whether to place the funds in the IOLTA account and does not designate who will receive the interest generated by the account. *See* Rev.Rul. 81-209, 1981-2 Cum.Bull. 16; Rev.Rul. 87-2, 1987-1 Cum.Bull. 18.

Respondents are the Washington Legal Foundation (WLF), Michael Mazzone, and William Summers. WLF is a public-interest law and policy center with members in the State of Texas who are opposed to the Texas IOLTA program. App. 26. Mazzone is an attorney admitted to practice in Texas who maintains an IOLTA account into which he regularly deposits client funds. *Id.* at 82. Summers is a Texas citizen and businessman whose work requires him to make regular use of the services of an attorney. In January 1994, Summers learned that a retainer he had deposited with his attorney was being held in an IOLTA account. *Id.* at 85. In February 1994, respondents filed this suit against petitioners – TEAJF, W. Frank Newton, in his official capacity as chairman of TEAJF, and the nine Justices of the Supreme Court of Texas. Respondents alleged, *inter alia,* that the Texas IOLTA program violated their rights under the Fifth Amendment, by taking their property without just compensation.

The District Court granted summary judgment to petitioners, reasoning that respondents had no property interest in the interest proceeds generated by the funds held in IOLTA accounts. *Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 873 F.Supp. 1 (W.D.Tex.1995). The Court of Appeals for the Fifth Circuit reversed, concluding that "any interest that accrues belongs to the owner of the principal." *Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 94 F.3d 996, 1004 (1996). Because of a split over whether the interest income generated by funds held in IOLTA accounts

is private property for purposes of the Fifth Amendment's Takings Clause,[3] we granted certiorari. 521 U.S. 1117, 117 S.Ct. 2535, 138 L.Ed.2d 1011 (1997).

II

The Fifth Amendment, made applicable to the States through the Fourteenth Amendment, *Chicago, B. & Q. R. Co. v. Chicago,* 166 U.S. 226, 239, 17 S.Ct. 581, 585-586, 41 L.Ed. 979 (1897), provides that "private property" shall not "be taken for public use, without just compensation." Because the Constitution protects rather than creates property interests, the existence of a property interest is determined by reference to "existing rules or understandings that stem from an independent source such as state law." *Board of Regents of State Colleges v. Roth,* 408 U.S. 564, 577, 92 S.Ct. 2701, 2709, 33 L.Ed.2d 548 (1972).

All agree that under Texas law the principal held in IOLTA trust accounts is the "private property" of the client. Texas IOLTA Rule 4 (discussing circumstances under which "client funds" must be deposited in an IOLTA account); Texas Bar Rule 1.14(a) (lawyers "shall hold funds . . . belonging in whole or in part to clients . . . separate from the lawyer's own property"); *see also* Brief for United States as *Amicus Curiae* 10 ("There can be no doubt that the client funds underlying the IOLTA program are the property of respondents"). When deposited in an IOLTA account, these funds remain in the control of a private attorney and are freely available to the client upon demand. As to the

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[3] *Cone v. State Bar of Fla.,* 819 F.2d 1002 (C.A.11), cert. denied, 484 U.S. 917, 108 S.Ct. 268, 98 L.Ed.2d 225 (1987); *In re Interest on Lawyers' Trust Accounts,* 672 P.2d 406 (Utah 1983); *Petition of New Hampshire Bar Assn.,* 122 N.H., at 975-976, 453 A.2d, at 1260-1261; *In re Minnesota State Bar Assn.,* 332 N.W.2d 151, 158 (Minn.1982); *In re Interest on Trust Accounts,* 402 So.2d 389, 395-396 (Fla.1981).

principal, then, the IOLTA rules at most "regulate the use of [the] property." *Yee v. Escondido,* 503 U.S. 519, 522, 112 S.Ct. 1522, 1526, 118 L.Ed.2d 153 (1992). Respondents do not contend that the State's regulation of the manner in which attorneys hold and manage client funds amounts to a taking of private property. The question in this case is whether the interest on an IOLTA account is "private property" of the client for whom the principal is being held.[4]

The rule that "interest follows principal" has been established under English common law since at least the mid-1700's. *Beckford v. Tobin,* 1 Ves.Sen. 308, 310, 27 Eng.Rep. 1049, 1051 (Ch. 1749) ("[I]nterest shall follow the principal, as the shadow the body"). Not surprisingly, this rule has become firmly embedded in the common law of the various States.[5] The Court of Appeals in this case, two of the three

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[4] We granted certiorari in this case to answer the question whether "interest earned on client trust funds held by lawyers in IOLTA accounts [is] a property interest of the client or lawyer, cognizable under the. . . Fifth Amendmen[t] to the U.S. Constitution. . . ." Pet. for Cert. i. Justice SOUTER contends that we should vacate the judgment of the Court of Appeals because it was improper for that court to have answered this question apart from the takings and just compensation questions. Petitioners, however, did not argue in their petition for certiorari that it was error for the Fifth Circuit to address the property question alone. Because, under this Court's Rule 14(1)(a), our practice is to consider "[o]nly the questions set forth in the petition, or fairly included therein," it would be improper for us *sua sponte* to raise and address the question answered by Justice SOUTER.

[5] *E.g., Freeman v. Young,* 507 So.2d 109, 110 (Ala.Civ.App.1987) ("The earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property" (internal quotation marks omitted)); *Pomona City School Dist. v. Payne,* 9 Cal.App.2d 510, 512, 50 P.2d 822, 823 (1935) ("[O]bviously the interest accretions belong to such owner"); *Vidal Realtors of Westport, Inc. v. Harry Bennett & Assocs., Inc.,* 1 Conn.App. 291, 297-298, 471 A.2d 658, 662 (1984) ("As long as the attached fund is used for profit, the profit . . . is impounded for the benefit of the attaching creditor and is subject to the same ultimate disposition as the principal of which it is the incident" (internal quotation

(continued...)

(footnote continued)

marks omitted)); *Burnett v. Brito,* 478 So.2d 845, 849 (Fla.App.1985) ("[A]ny interest earned on interpleaded and deposited funds follows the principal and shall be allocated to whomever is found entitled to the principal"); *Morton Grove Park Dist. v. American Nat. Bank & Trust Co.,* 78 Ill.2d 353, 362-363, 35 Ill.Dec. 767, 771, 399 N.E.2d 1295, 1299 (1980) ("The earnings on the funds deposited are a mere incident of ownership of the fund itself "); *B & M Coal Corp. v. United Mine Workers,* 501 N.E.2d 401, 405 (Ind.1986) ("[I]nterest earnings must follow the principal and be distributed to the ultimate owners of the fund"); *Unified School Dist. No. 490, Butler County v. Board of County Commissioners of Butler County,* 237 Kan. 6, 9, 697 P.2d 64, 69 (1985) ("[I]nterest follows principal"); *Pontiac School Dist. v. City of Pontiac,* 294 MiCh. 708, 715-716, 294 N.W. 141, 144 (1940) ("The generally understood and applied principles that interest is merely an incident of the principal and must be accounted for"); *State Highway Comm'n v. Spainhower,* 504 S.W.2d 121, 126 (Mo.1973) ("Interest earned by a deposit of special funds is an increment accruing thereto" (internal quotation marks omitted)); *Siroky v. Richland County,* 271 Mont. 67, 74, 894 P.2d 309, 313 (1995) ("[I]nterest earned belongs to the owner of the funds that generated the interest"); *Bordy v. Smith,* 150 Neb. 272, 276, 34 N.W.2d 331, 334 (1948) ("Once settled clearly and definitely whose money the principal sum was, the interest necessarily belongs to that person as an increment to the principal fund"); *State ex rel. Board of County Commissioners v. Montoya,* 91 N.M. 421, 423, 575 P.2d 605, 607 (1978) ( "[T]he general rule is that interest is an accretion or increment to the principal fund earning it"); *Stuarco, Inc. v. Slafbro Realty Corp.,* 30 A.D.2d 80, 82, 289 N.Y.S.2d 883, 885 (1968) (plaintiff "is entitled to the interest actually accrued . . . despite the absence of any agreement to pay interest on the deposit, and this precisely and only because interest was in fact earned thereon"); *McMillan v. Robeson County,* 262 N.C. 413, 417, 137 S.E.2d 105, 108 (1964) ("The earnings on the fund are a mere incident of ownership of the fund itself"); *Des Moines Mut. Hail & Cyclone Ins. Assn. v. Steen,* 43 N.D. 298, 301, 175 N.W. 195 (1919) ( "[A]ccruing interest follows the principal"); *Board of Educ., Woodward Public Schools v. Hensley,* 665 P.2d 327, 331 (Okla.App.1983) ("The interest earned . . . becomes a part of the principal of the fund which generates it"); *University of S.C. v. Elliott,* 248 S.C. 218, 220, 149 S.E.2d 433, 434 (1966) ("[I]nterest earned ... is simply an increment of the principal fund, making the interest the property of the party who owned the principal fund"); *Board of County Commissioners of the County of Laramie v. Laramie County School Dist. No. One,* 884

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judges of which are Texans, held that Texas also follows this rule, citing *Sellers v. Harris County,* 483 S.W.2d 242, 243 (Tex.1972) ("The interest earned by deposit of money owned by the parties to the lawsuit is an increment that accrues to that money and to its owners"). Indeed, in *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 162, 101 S.Ct. 446, 451, 66 L.Ed.2d 358 (1980), we cited the *Sellers* opinion as demonstrative of the general rule that "any interest . . . follows the principal."

In *Webb's,* we addressed a Florida statute providing that interest accruing on an interpleader fund deposited in the registry of the court "'shall be deemed income of the office of the clerk of the circuit court.'" *Id.* at 156, n. 1, 101 S.Ct., at 448, n. 1 (quoting Fla. Stat. § 28.33 (1977)) (emphasis deleted). The appellant in that case filed an interpleader action in Florida state court and tendered the sum at issue, nearly $2 million, into court. In addition to deducting $9,228.74 from the interpleader fund as a fee "for services rendered," the clerk of court also retained the more than $100,000 in interest income generated by the deposited funds. We held that the statute authorizing the clerk to confiscate the earned interest violated the Takings Clause. As we explained, "a State, by *ipse dixit,* may not transform private property into public property without compensation" simply by legislatively abrogating the traditional rule that "earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property." 449 U.S., at 164, 101 S.Ct., at 452. In other words, at least as to confiscatory regulations (as opposed to those regulating the use of property), a State may not sidestep the Takings Clause

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(footnote continued)

P.2d 946, 953 (Wyo.1994) ("In general, interest is merely an incident of the principal fund, making it the property of the party owning the principal fund").

by disavowing traditional property interests long recognized under state law. *See id.*, at 163-164, 101 S.Ct., at 451-453; *see also Lucas v. South Carolina Coastal Council,* 505 U.S. 1003, 1029, 112 S.Ct. 2886 2900-2901, 120 L.Ed.2d 798 (1992).

Petitioners nevertheless contend that *Webb's* does not control because Texas does not, in fact, adhere to the "interest follows principal" rule, "at least if elevated to the level of an absolute legal rule." Brief for Petitioners 22. They point to several examples, such as income-only trusts and marital community property rules, where under Texas law interest does not follow principal. According to petitioners, the IOLTA program is simply another exception to the general rule.

We find these examples insufficient to dispel the presumption of deference given the views of a federal court as to the law of a State within its jurisdiction. *Bernhardt v. Polygraphic Co. of America,* 350 U.S. 198, 204, 76 S.Ct. 273, 276-277, 100 L.Ed. 199 (1956). Petitioners' examples miss the point of our decision in *Webb's.* Texas' exception of income-only trusts and certain marital property from the general rule that "interest follows principal" has a firm basis in traditional property law principles. Permitting the owner of a sum of money to distribute to a designated beneficiary the interest income generated by his principal is entirely consistent with the fundamental maxim of property law that the owner of a property interest may dispose of all or part of that interest as he sees fit. *United States v. General Motors Corp.,* 323 U.S. 373, 377-378, 65 S.Ct. 357, 359, 89 L.Ed. 311 (1945) (property "denote[s] the group of rights inhering in the citizen's relation to the physical thing, as the right to . . . dispose of it"). Similarly, the Texas rules governing the distribution of marital assets have a historical pedigree tracing back to the marital property laws adopted by the Texas Congress only four years after Texas became an

independent republic. W. McClanahan, Community Property Law in the United States § 3:23, pp. 123-124 (1982). But petitioners point to no "background principles" of property law, *Lucas, supra,* at 1030, 112 S.Ct., at 2901, that would lead one to the conclusion that the owner of a fund temporarily deposited in an attorney trust account may be deprived of the interest the fund generates.

Petitioners further contend that "interest follows principal" is an incomplete explication of the Texas rule. Reply Brief for Petitioners 11. Petitioners explain that interest follows principal in Texas only if the interest is "allowed by law or fixed by the parties." *Cavnar v. Quality Control Parking, Inc.,* 696 S.W.2d 549, 552 (Tex.1985). We fail to see how this assists petitioners' cause. We agree that the government has great latitude in regulating the circumstances under which interest may be earned. As we explained in *Andrus v. Allard,* 444 U.S. 51, 66, 100 S.Ct. 318, 327, 62 L.Ed.2d 210 (1979), "anticipated gains ha[ve] traditionally been viewed as less compelling than other property-related interests." But petitioners do not argue that the payment of interest on client funds deposited in an attorney trust account is not "allowed by law" in Texas. Rather, they argue that interest actually "earned" by funds held in IOLTA accounts, Texas IOLTA Rule 9, is not the private property of the owner of the principal. However, regardless of whether the owner of the principal has a constitutionally cognizable interest in the *anticipated* generation of interest by his funds, any interest that *does* accrue attaches as a property right incident to the ownership of the underlying principal.

Finally, petitioners argue that the interest income transferred to the TEAJF is not "private property" because the client funds held in IOLTA accounts "cannot reasonably be expected to generate interest income on their own." Brief for Petitioners 18. As an initial matter, petitioners' assertion

that client funds held in IOLTA accounts cannot be expected to generate interest income is plainly incorrect under the express terms of the Texas IOLTA rules. Texas IOLTA Rule 6 requires that client funds held by an attorney be deposited in an IOLTA account "if the interest which might be earned" is insufficient to offset the "cost of establishing and maintaining the account, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain the interest on such funds for the client." In other words, it is not that the client funds to be placed in IOLTA accounts cannot generate *interest,* but that they cannot generate *net interest.*

Whether client funds held in IOLTA accounts could generate net interest is a matter of some dispute. As written, the Texas IOLTA program requires the calculation as to net interest to be made "without regard to funds of other clients which may be held by the attorney." Texas IOLTA Rule 6. This provision would deny to an attorney the traditional practice of pooling funds of several clients in one account, a practice which might produce net interest when opening an account for each client would not. But in the District Court, petitioners agreed that this portion of the rule was not to be enforced, and that an attorney could make the necessary calculation on the basis of pooled accounts. Petitioners made a similar concession during oral argument here. Tr. of Oral Arg. 13-16. We accept this concession but find that it does not avail petitioners.

We have never held that a physical item is not "property" simply because it lacks a positive economic or market value. For example, in *Loretto v. Teleprompter Manhattan CATV Corp.,* 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982), we held that a property right was taken even when infringement of that right arguably *increased* the market value of the property at issue. *Id.,* at 437, n. 15, 102 S.Ct., at 3177, n. 15. Our conclusion in this regard was

premised on our longstanding recognition that property is more than economic value, *see id.,* at 435, 102 S.Ct., at 3175-3176; it also consists of "the group of rights which the so-called owner exercises in his dominion of the physical thing," such "as the right to possess, use and dispose of it," *General Motors, supra,* at 378, 65 S.Ct., at 359. While the interest income at issue here may have no economically realizable value to its owner, possession, control, and disposition are nonetheless valuable rights that inhere in the property. *See Hodel v. Irving,* 481 U.S. 704, 715, 107 S.Ct. 2076, 2083, 95 L.Ed.2d 668 (1987) (noting that "the right to pass on" property "is itself a valuable right"). The government may not seize rents received by the owner of a building simply because it can prove that the costs incurred in collecting the rents exceed the amount collected.

The United States, as *amicus curiae,* additionally argues that "private property" is not implicated by the IOLTA program because the interest income generated by funds held in IOLTA accounts is "government-created value." Brief for United States as *Amicus Curiae* 20. We disagree. As an initial matter, this argument is factually erroneous. The interest income transferred to the TEAJF is not the product of increased efficiency, economies of scale, or pooling of funds by the government. Indeed, as noted above, the State has conceded at oral argument that if an attorney could in any way (such as pooling of client funds) earn interest for a client, he is ethically obligated to do so rather than place the funds in an IOLTA account. Interest income is economically realizable by IOLTA primarily because: (1) the Federal Government imposes tax reporting costs only on those who attempt to exercise control over the interest their funds generate, *see* Rev.Rul. 81-209, 1981-2 Cum.Bull. 16; Rev.Rul. 87-2, 1987-1 Cum.Bull. *18;* and (2) the Federal Government prohibits for-profit corporations from holding funds in NOW accounts if the interest is paid to the corporation, but permits corporate funds to be held in

NOW accounts if the interest is paid to the TEAJF, *see* Federal Reserve's IOLTA Letter. In other words, the State does nothing to create value; the value is created by respondents' funds. The Federal Government, through the structuring of its banking and taxation regulations, imposes costs on this value if private citizens attempt to exercise control over it. Waiver of these costs if the property is remitted to the State hardly constitutes "government-created value."

In any event, we rejected a similar "government-created value" argument in *Webb's.* There, the State of Florida argued that since the clerk's authority to invest deposited funds was a statutorily created right, any interest income generated by the funds was not private property. 449 U.S., at 163, 101 S.Ct., at 451-452. We rejected this argument, explaining that "the State's having mandated the accrual of interest does not mean the State or its designate is entitled to assume ownership of the interest." *Id.,* at 162, 101 S.Ct., at 451.

This would be a different case if the interest income generated by IOLTA accounts was transferred to the State as payment "for services rendered" by the State. *Id.,* at 157, 101 S.Ct., at 448-449. Our holding does not prohibit a State from imposing reasonable fees it incurs in generating and allocating interest income. *See id.,* at 162, 101 S.Ct., at 451; cf. *United States v. Sperry Corp.,* 493 U.S. 52, 60, 110 S.Ct. 387, 393-394, 107 L.Ed.2d 290 (1989) (upholding the imposition of a "reasonable 'user fee' " on those utilizing the Iran-United States Claims Tribunal). But here the State does not, indeed cannot, argue that its confiscation of respondents' interest income amounts to a fee for services performed. Unlike in *Webb's,* where the State safeguarded and invested the deposited funds, funds held in IOLTA accounts are managed entirely by banks and private attorneys.

III.

In sum, we hold that the interest income generated by funds held in IOLTA accounts is the "private property" of the owner of the principal. We express no view as to whether these funds have been "taken" by the State; nor do we express an opinion as to the amount of "just compensation," if any, due respondents. We leave these issues to be addressed on remand. The judgment of the Court of Appeals is

Affirmed.

Justice SOUTER, with whom Justice STEVENS, Justice GINSBURG, and Justice BREYER join, dissenting.

The Court holds that "interest income generated by funds held in IOLTA accounts is the 'private property' of the owner of the principal." *Ante,* this page. I do not join in today's ruling because the Court's limited enquiry has led it to announce an essentially abstract proposition; even assuming that the proposition correctly states the law, it may ultimately turn out to have no significance in resolving the real issue raised in this case, which is whether the Interest on Lawyers Trust Account (IOLTA) scheme violates the Takings Clause of the Fifth Amendment. Since the sounder course would be to vacate the similarly limited judgment of the Court of Appeals for the Fifth Circuit and remand for the broader enquiry outlined below, I respectfully dissent.

The Court recognizes three distinct issues implicated by a takings claim: whether the interest asserted by the plaintiff is property, whether the government has taken that property, and whether the plaintiff has been denied just compensation for the taking. *Ibid.* The Court is careful to address only the first of these questions, *ibid.,* which is the only one on which the Fifth Circuit ruled. *See Washington Legal Foundation v. Texas Equal Access to Justice Foundation,* 94 F.3d 996, 1004 (1996).

The affirmative answer given by the Court and the Fifth Circuit to the question whether IOLTA interest attributable to a client's funds is the client's property states, in essence, a proposition of state law, which is one source of property interests entitled to federal constitutional protection, *see Board of Regents of State Colleges v. Roth,* 408 U.S. 564, 577, 92 S.Ct. 2701, 2709, 33 L.Ed.2d 548 (1972), and *Lucas v. South Carolina Coastal Council,* 505 U.S. 1003, 1030, 112 S.Ct. 2886, 2901, 120 L.Ed.2d 798 (1992). In this instance the relevant state law is said to embrace the general principle that property in interest income follows ownership of the principal on which the interest is earned, *ante,* at 1930, and n. 4, and the Court treats any income generated by a client's funds like income that the client could derive directly through a method of money management or investment that costs more than it produced, *ante,* at 1932-1933.

In addressing only the issue of the property interest, leaving the questions of taking and compensation for a later day in the litigation of respondents' action, the Court and the Court of Appeals have, however, postponed consideration of the most salient fact relied upon by petitioners in contesting respondents' Fifth Amendment claim: that the respondent client would effectively be barred from receiving any net interest on his funds subject to the state IOLTA rule by the combination of an unchallenged federal banking statute and regulation, 12 U.S.C. § 1832(a); 12 CFR § 204.130 (1997); a separate, unchallenged Texas rule of attorney discipline, Texas Bar Rules, Art. 10, § 9, Rule 1.14(b); and unchallenged Internal Revenue Service interpretations of the Tax Code, Rev.Rul. 81-209, 1981-2 Cum.Bull. 16; Rev.Rul. 87-2, 1987-1 Cum.Bull. 18. The argument for the view contrary to the one taken by the Court would emphasize that salient fact right now. The view that the client has no

cognizable property right in the IOLTA interest is said to rest not only on a different understanding of the scope of the general principle and its place in state law,[1] but also upon the very regulatory framework that would prevent a client from obtaining any net interest on funds now subject to IOLTA, even if IOLTA did not exist.[2] It is not, of course, that the federal and state regulatory combination includes some rule that is facially inconsistent with the general principle that interest follows principal; the components of the regulatory structure do not even directly address the question of who owns interest. Indeed, the most obvious relevance of the regulatory provisions and their effects is to the issues of whether IOLTA results in a taking of the client's property and whether any such taking requires compensation. And yet by this route the regulatory structure becomes relevant to the property issue as well, simply because the way we may ultimately resolve the taking and compensation issues bears on the way we ought to resolve the property issue. If it should turn out that within the meaning of the Fifth Amendment, the IOLTA scheme had not taken the property recognized today, or if it should turn out that the "just compensation" for any taking was zero, then there would be

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[1] The highest court of Texas has not understood the general principle that a property right in interest always follows property in principle in a way that supports respondents in this IOLTA challenge. *See Sellers v. Harris County,* 483 S.W.2d 242, 243 (Tex.1972) (owner of principal is entitled to interest, less administrative and accounting costs). *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980), is not on point precisely because it dealt with interest actually in the hands of the fiduciary, net of any administrative expense.

[2] These unchallenged state and federal rules clearly fall within the general category of relevant law defining property subject to constitutional protection, *see Board of Regents of State Colleges v. Roth,* 408 U.S. 564, 577, 92 S.Ct. 2701, 2709, 33 L.Ed.2d 548 (1972) ( "Property interests" are "created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law").

no practical consequence for purposes of the Fifth Amendment in recognizing a client's property right in the interest in the first place; any such recognition would be an inconsequential abstraction. *Cf. Hooker v. Burr,* 194 U.S. 415, 419, 24 S.Ct. 706, 708, 48 L.Ed. 046 (1904) (If a contractual obligation is impaired, but the obligor is "not injured to the extent of a penny thereby, his abstract rights are unimportant"). The significance of the regulatory structure, and the issues of taking and compensation, should therefore be considered today.

Approaching the property issue in conjunction with the two others would, in fact, be entirely faithful to the Fifth Amendment, for as we have repeatedly said its Takings Clause does nothing to bar the government from taking property, but only from taking it without just compensation, *see, e.g., First English Evangelical Lutheran Church of Glendale v. County of Los Angeles,* 482 U.S. 304, 315, 107 S.Ct. 2378, 2385-2386, 96 L.Ed.2d 250 (1987); *Williamson County Regional Planning Comm'n v. Hamilton Bank of Johnson City,* 473 U.S. 172, 194, 105 S.Ct. 3108, 3120-3121, 87 L.Ed.2d 126 (1985). It thus makes good sense to consider what is property only in connection with what is a compensable taking, an approach to Fifth Amendment analysis that not only would avoid spending time on what might turn out to be an entirely theoretical matter, but would also reduce the risk of placing such undue emphasis on the existence of a generalized property right as to distort the taking and compensation analyses that necessarily follow before the Fifth Amendment's significance can be known. [3]

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[3] For example, with respect to the determination whether government regulation "goes too far" in diminishing the value of a claimant's property, we have repeatedly instructed that a "parcel of property could not first be divided into what was taken and what was left for the purpose of demonstrating the taking of the former to be complete and hence

(continued...)

That is not to say, of course, that we should resolve either the taking or compensation issues here, for the Fifth Circuit did not address them. Rather, we should determine here whether either of the remaining issues might reasonably be resolved against respondents; if so, we should not abstract the property issue for resolution in their favor now, but should return the case to the Court of Appeals to consider all three issues before resolving the first. Suffice it to say that both the taking and compensation questions are serious ones for respondents.

First, as to a taking, we start with *Penn Central Transp. Co. v. New York City,* 438 U.S. 104, 98 S.Ct. 2646, 57 L.Ed.2d 631 (1978), and its guidance about certain sorts of facts that are of particular importance in what is supposed to be an "ad hoc, factual" enquiry, *id.,* at 124, 98 S.Ct., at 2659, into whether the government has "go[ne] too far." *Pennsylvania Coal Co. v. Mahon,* 260 U.S. 393, 415, 43 S.Ct. 158, 160, 67 L.Ed. 322 (1922). Attention should be paid to the nature of the government's action, its economic impact, and the degree of any interference with reasonable, investment-backed expectations. *Penn Central, supra,* at 124, 98 S.Ct., at 2659. Here it is enough to note the possible significance of the facts that there is no physical occupation or seizure of tangible property, *cf. Loretto v. Teleprompter Manhattan CATV Corp.,* 458 U.S. 419, 426, 102 S.Ct. 3164,

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(footnote continued)

compensable." *Concrete Pipe & Products of Cal., Inc. v. Construction Laborers Pension Trust for Southern Cal.,* 508 U.S. 602, 644, 113 S.Ct. 2264, 2290, 124 L.Ed.2d 539 (1993); *see also Penn Central Transp. Co. v. New York City,* 438 U.S. 104, 130-131, 98 S.Ct. 2646, 2662- 2663, 57 L.Ed.2d 631 (1978). With its narrow focus on a party's right to any interest generated by its principal, the Court's opinion might be read (albeit erroneously, in my view) to mean that the accrued interest is the only property right relevant to the question whether IOLTA effects a taking.

3170-3171, 73 L.Ed.2d 868 (1982) (noting that physical intrusion is "unusually serious" in the takings context); that there is no apparent economic impact (since the client would have no net interest to go in his pocket, IOLTA or no IOLTA); and that the facts present neither anything resembling an investment nor (for the reason just given) any apparent basis for reasonably expecting to obtain net interest. While a court would certainly consider any proposal that respondents might make for a departure from the *Penn Central* approach to vindicating the Fifth Amendment in these circumstances, application of *Penn Central* would not bode well for claimants like respondents.

Second, as to the just compensation requirement, the client's inability to earn net interest outside IOLTA, due to the unchallenged federal and state regulations, raises serious questions about entitlement to any compensation (which, if required, would convert any "taking" into a wash transaction from the client's standpoint). "Just compensation" generally means "the full monetary equivalent of the property taken." *United States v. Reynolds,* 397 U.S. 14, 16, 90 S.Ct. 803, 805, 25 L.Ed.2d 12 (1970). In determining the amount of just compensation for a taking, a court seeks to place a claimant "'in as good a position pecuniarily as if his property had not been taken.'" *United States v. 564.54 Acres Land,* 441 U.S. 506, 510, 99 S.Ct. 1854, 1857, 60 L.Ed.2d 435 (1979) (quoting *Olson v. United States,* 292 U.S. 246, 255, 54 S.Ct. 704, 708, 78 L.Ed. 1236 (1934)), calculating any loss objectively and independently of the claimant's subjective valuation, *see, e.g., Kimball Laundry Co. v. United States,* 338 U.S. 1, 5, 69 S.Ct. 1434, 1437-1438, 93 L.Ed. 1765 (1949).

Thus, in deciding what award would be needed to place the client respondent in as good a position as he would have enjoyed without a taking, a court presumably would look to the claimant's putative property interest as it was or

would have been enjoyed in the absence of IOLTA, *cf. Boston Chamber of Commerce v. Boston,* 217 U.S. 189, 195, 30 S.Ct. 459, 460-461, 54 L.Ed. 725 (1910), and consequently would measure any required compensation by the claimant's loss, not by the government's (or the public's) gain, *ibid.* This rule would not obviously produce much benefit to respondents. While it has been suggested in their favor that a cognizable taking may occur even when value has been enhanced, on the supposed authority of *Loretto, supra,* at 437, n. 15, 102 S.Ct., at 3177, n. 15, that case dealt only with physical occupation, it rested on no finding that value had actually been enhanced, and it held nothing about the legal consequences of an actual finding that enhancement had occurred. The Court today makes a further suggestion of a way in which respondents might deflect the objection that they have lost nothing, when it observes that the notion of property is not limited by the concept of value, *ante,* at 1933. But the Court makes the point by equating the government's seizure of funds from the pocket of a failing business owner with IOLTA's disposition of funds the client never had or could have received. Neither the equation, nor its relevance to the Fifth Amendment's guarantee of just compensation, is immune to question.

But, however these issues of taking and compensation may someday be adjudicated, two things are clear now: the issues are serious and they might be resolved against respondents. If that should happen, today's holding would stand as an abstract proposition without significance for the application of the Fifth Amendment.

If abstraction were guaranteed to be harmless, of course, an abstract ruling now and again would not matter much, beyond the time spent reaching it. But our law has been wary of abstract legal propositions not only because the common-law tradition is a practical one, but because abstractions pose their own peculiar risks. As THE CHIEF

JUSTICE noted in a different but related context, there is a danger in "cutting loose the notion of 'just compensation' from the notion of 'private property.'" *Almota Farmers Elevator & Warehouse Co. v. United States,* 409 U.S. 470, 486, 93 S.Ct. 791, 800, 35 L.Ed.2d 1 (1973) (REHNQUIST, J., dissenting); *see also id.,* at 482-483, 93 S.Ct., at 798-799 ("While the inquiry as to what property interest is taken by the condemnor and the inquiry as to how that property interest shall be valued are not identical ones, they cannot be divorced without seriously undermining a number of rules dealing with the law of eminent domain").

One may wonder here not only whether the theoretical property analysis may skew the resolution of the taking and compensation issues that will follow, but also how far today's holding may unsettle accepted governmental practice elsewhere. By recognizing an abstract property right to interest "actually 'earned'" by a party's principal, *ante,* at 1932, does the Court not raise the possibility of takings challenges whenever the government holds and makes use of the principal of private parties, as it frequently does? When, for example, the National Government, or a State, has engaged in excessive tax withholding, it does not refund the interest earned between the time of withholding and the issuance of a refund. For any number of reasons unrelated to the recognition or nonrecognition of a generalized property right in interest, but tied to the questions of takings and compensation, it seems unlikely that such withholding practices would violate the Fifth Amendment. Nevertheless, the Court's abstract ruling may encourage claims of just this sort.

To avoid the dangers of abstraction, I would therefore vacate the judgment of the Court of Appeals and remand for plenary Fifth Amendment consideration. If, however, the property interest question is to be considered in the abstract, I

would recast it and answer it as Justice BREYER has done in his own dissenting opinion, which I join.

Justice BREYER, with whom Justice STEVENS, Justice SOUTER, and Justice GINSBURG join, dissenting.

The question presented is whether "interest earned on client trust funds," which would "not earn interest" in the absence of a special "IOLTA program," amounts to a "property interest of the client or lawyer" for purposes of the Fifth Amendment's Takings Clause. Brief for Petitioners i; Brief for Respondents i; *see* U.S. Const., Amdt. 5 ("nor shall private property be taken for public use, without just compensation").

The question presented is premised on four assumptions: First, that lawyers sometimes hold small amounts of clients' funds for short periods of time; second, that because of federal tax and banking rules and regulations, such funds normally could not earn interest during that time; third, that state Interest on Lawyers Trust Account (IOLTA) rules require lawyers to place such funds in a special account where, mixed with other funds, they will earn interest; and fourth, that IOLTA rules require that interest earned on these funds is distributed to groups that represent low-income individuals rather than to the lawyers or their clients who own the funds.

Insofar as factual circumstances such as these raise a Fifth Amendment question, I agree with Justice SOUTER that the question is whether Texas, by requiring the placing of the funds in special IOLTA accounts and depriving the funds' owners of the subsequently earned interest has temporarily "taken" what is undoubtedly "private property," namely, the client's funds, *i.e.,* the principal, without "just compensation." To answer this (appropriately framed) question, the parties and the lower courts would have to consider whether the use of the principal in the fashion dictated by the IOLTA rules amounts to a deprivation of a

property right, and, if so, whether the government's "taking" required compensating the owner of the funds, where it did not deprive the funds' owners of interest they might have otherwise received. But the Court of Appeals did not address this latter question. *See ante,* at 1937 (SOUTER, J., dissenting).

Although I believe it wrong to separate Takings Clause analysis of the property rights at stake from analysis of the alleged deprivation, I have considered the question presented on its own terms. And, on the majority's assumptions, I believe that its answer is not the right one. The majority's answer rests upon the use of a legal truism, namely, "interest follows principal," and its application of a particular case, namely, *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980). *See ante,* at 1931-1932, 1933-1934. In my view, neither truism nor case can answer the hypothetical question the Court addresses.

The truism does not help because the question presented assumes circumstances that differ dramatically from those in which interest is ordinarily at issue. Ordinarily, principal is capable of generating interest for whoever holds it. Here, by the very terms of the question, we must assume that (because of pre-existing federal law) the client's principal could not generate interest without IOLTA intervention. That is to say, the client could not have had an expectation of receiving interest without that intervention. Nor can one say that IOLTA rules excluded, or prevented, the client's use of his principal to generate interest that would otherwise be his. Under these circumstances, what is the property right of the client that IOLTA could have "confiscat[ed]"? *Ante,* at 1932.

The most that Texas law here could have taken from the client is not a right to use his principal to create a benefit (for he had no such right), but the client's right to keep the

client's principal sterile, a right to prevent the principal from being put to productive use by others. *Cf. National Bd. of YMCA v. United States,* 395 U.S. 85, 92-93, 89 S.Ct. 1511, 1515-1516, 23 L.Ed.2d 117 (1969) (noting that government deprivation of property requiring compensation normally takes from an owner *use* that the owner may otherwise make of the property). And whatever this Court's cases may have said about the constitutional status of such a right, they have *not* said that the Constitution forces a State to confer, upon the owner of property that cannot produce anything of value for him, ownership of the fruits of that property should that property be rendered fertile through the government's lawful intervention. *Cf., e.g., United States ex rel. TVA v. Powelson,* 319 U.S. 266, 276, 63 S.Ct. 1047, 1053, 87 L.Ed. 1390 (1943) (no need to pay for value that the "power of eminent domain" itself creates); *City of New York v. Sage,* 239 U.S. 57, 61, 36 S.Ct. 25, 26, 60 L.Ed. 143 (1915) (city need not pay for value added by unifying parcels where unification impracticable absent eminent domain); *United States v. Twin City Power Co.,* 350 U.S. 222, 228, 76 S.Ct. 259, 263, 100 L.Ed. 240 (1956) (to require payment for value created by government "would be to create private claims in the public domain"). Thus the question is whether "interest," *earned only as a result of IOLTA rules* and earned upon otherwise *barren* client principal, "follows principal." The slogan "interest follows principal" no more answers *that* question than does King Diarmed's legendary slogan, "[T]o every cow her calf." A. Birrell, Seven Lectures on The Law and History of Copyright in Books 42 (1889) (internal quotation marks omitted). *Cf. Berkey v. Third Avenue Railway Co.,* 244 N.Y. 84, 94, 155 N.E. 58, 61 (1926) (Cardozo, J.) ("Metaphors in law are to be narrowly watched, for starting as devices to liberate thought, they end often by enslaving it").

Nor can *Webb's Fabulous Pharmacies* answer the question presented. But for state intervention the principal in

that case could have, and would have, earned interest. *See* 449 U.S., at 156-157, and nn. 1, 2, 101 S.Ct., at 448, and nn. 1, 2 (state law required party to deposit funds with court, authorized court to hold the funds in an interest-bearing account, and allowed the court to claim the interest as well as a fee). Here, federal law ensured that, in the absence of IOLTA intervention, the client's principal would earn nothing. *Webb's Fabulous Pharmacies* holds that a state law which places *that* ordinary kind of principal in an interest-bearing account (which interest the State unjustifiably keeps) takes "private property . . . for public use without just compensation." That holding says little about *this* kind of principal, principal that otherwise is barren. Nor do cases that find a private interest in property with virtually no economic value tell us to *whom* the fruits of that property belong when that property bears fruit through the intervention of another. *Ante,* at 1933 (citing *Loretto v. Teleprompter Manhattan CATV Corp.,* 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982); *Hodel v. Irving,* 481 U.S. 704, 715, 107 S.Ct. 2076, 2082-2083, 95 L.Ed.2d 668 (1987)).

If necessary, I should find an answer to the question presented in other analogies that this Court's precedents provide. Land valuation cases, for example, make clear that the value of what is taken is bounded by that which is "lost," not that which the "taker gained." *Boston Chamber of Commerce v. Boston,* 217 U.S. 189, 195, 30 S.Ct. 459, 460-461, 54 L.Ed. 725 (1910) (opinion of Holmes, J.); *see also United States v. Miller,* 317 U.S. 369, 375, 63 S.Ct. 276, 280-281, 87 L.Ed. 336 (1943) ("[S]pecial value to the condemnor . . . must be excluded as an element of market value"); *United States v. Chandler-Dunbar Water Power Co.,*229 U.S. 53, 75-76, 33 S.Ct. 667, 676-677, 57 L.Ed. 1063 (1913). This principle suggests that the government must pay the current value of condemned land, not the added value that a highway it builds on the property itself creates. It also suggests that condemnation of, say, riparian rights in order to

build a dam must be followed by compensation for these rights, not for the value of the electricity that the dam would later produce. *Cf. id.*, at 76, 33 S.Ct., at 677; *Twin City Power Co., supra,* at 226-228, 76 S.Ct., at 261-263; *United States v. Appalachian Elec. Power Co.,* 311 U.S. 377, 423-424, 427, 61 S.Ct. 291, 306-307, 308-309, 85 L.Ed. 243 (1940). Indeed, no one would say that such electricity was, for Takings Clause purposes, the owner's "private property," where, as here, in the absence of the lawful government "taking," there would have been no such property.

These legal analogies more directly address the key assumption raised by the question presented, namely, that "absent the IOLTA program," no "interest" could have been earned. I consequently believe that the interest earned is *not* the client's "private property."

I respectfully dissent.

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 95-50160

WASHINGTON LEGAL FOUNDATION; William R. Summers; Michael J. Mazzone,

Plaintiffs-Appellants,

v.

TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; W. Frank Newton, Chairman, Texas Equal Access to Justice Foundation; Thomas R. Phillips, Chief Justice; Raul Gonzalez, Justice; Jack Hightower, Justice; Nathan L. Hecht, Justice; Lloyd A. Doggett, Justice; Bob Gammage, Justice; Craig T. Enoch, Justice; John Cornyn, Justice; Rose Spector, Justice; Supreme Court Dfts,

Defendants-Appellees.

September 12, 1996

Appeal from the United States District Court for the Western District of Texas.

Before WISDOM, GARWOOD and JONES, Circuit Judges.

WISDOM, Circuit Judge:

The plaintiffs-appellants appeal the district court's denial of their motion for summary judgment and the court's award of summary judgment to the defendants-appellees, in

which the district court upheld the constitutionality of the Texas statute, Interest on Lawyers Trust Accounts Program (IOLTA), and found that the defendants are entitled to limited immunity under the Eleventh Amendment. For the reasons that follow, we REVERSE the judgment of the district court in part, VACATE and remand in part, and AFFIRM in part.

## I.

### *Statement of Facts*

Clients often give their attorneys money to be held in escrow, such as retainer fees or closing costs for a transaction. In Texas, traditional ethical rules require attorneys to place this money in a trust account that permits withdrawal on demand. The ethical rules also allow attorneys to aggregate all client funds into a single trust account and prohibit attorneys from commingling their own money with the trust fund. Because federal law prohibited banks from paying interest on demand accounts,[1] these accounts formerly amounted to interest-free loans to the banks.

In 1980, new banking regulations allowed negotiable order of withdrawal (NOW) accounts,[2] which operate as interest-bearing checking accounts. NOW accounts created a vehicle for attorneys to pool client funds into an interest-bearing trust account, provided that none of the funds belong

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[1] S. REP. NO. 96-368, 9th Cong., 2d Sess. 5, *reprinted in* 1980 U.S.C.C.A.N. 240, 240.

[2] Depository Institutions Deregulation and Monetary Control Act of 1980, 94 Stat. 132, 146 (codified as amended at 12 U.S.C.A. § 1832 (West 1989)); *see also* S. Rep. No. 96-368, *reprinted in* 1980 U.S.C.C.A.N. at 242-43.

to a for-profit corporation.[3] Attorneys, however, may not deduct the costs of maintaining the trust account from the interest earned, because such a practice would constitute an impermissible benefit from the management of the trust account in violation of the ethical rules.

The creation of NOW accounts led to the development of IOLTA programs. The IOLTA concept arises from the premise that there are still situations in which, because of the nominal amount of a client's funds to be held or the brief period for which a client's funds will be held, NOW accounts are not feasible; the costs of maintaining such accounts outweigh the interest that each client would have earned. In these situations, the trust accounts still operated as interest-free loans to the banks. IOLTA is an attempt to switch this benefit from the banks to legal providers for the indigent.

Under its statutory power to regulate the state bar, the Texas Supreme Court created its IOLTA program in 1984, which is modeled after IOLTA programs used in other states and which seeks to capitalize on this banking anomaly. The IOLTA program originally permitted attorneys to place client funds that were "nominal in amount" or were "reasonably anticipated to be held for a short period of time" into an unsegregated interest-bearing bank account (IOLTA account), the interest of which is paid to the Texas Equal Access to Justice Foundation (TEAJF), a non-profit corporation created by the Texas Supreme Court.[4] At that

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[3] *See 12* U.S.C.A. § 1832(a)(2) (permitting NOW accounts to consist of commingled funds belonging to numerous individuals or non-profit organizations or both).

[4] *See* TEX.GOV'T CODE ANN. tit. 2, subtit. G, app. A, art. 11 § § 6- 7 (1987). Attorneys must make a reasonable determination as to whether a client's funds are nominal in amount or only to be held for a short period

(continued...)

time, Texas's IOLTA program was voluntary, meaning that an attorney could choose whether to participate but clients had no choice, other than to select an attorney who did not maintain an IOLTA account.

The TEAJF's purpose is to manage and distribute the interest earned from the IOLTA accounts to non-profit organizations that "have as a primary purpose the delivery of legal services to low income persons,"[5] with the exception that no funds may be used to finance class action lawsuits or to lobby on behalf of a political candidate or issue.[6] Nearly all states have similar systems, which were designed to provide much-needed finances to legal providers for the impoverished. States have drastically slashed the budgets for such programs over the years; in 1993, the Texas legislature even refused to enact a modest increase in court filing fees to compensate for temporary IOLTA shortfalls.

Initially, the Texas IOLTA program did not meet expectations. Attorneys were reluctant to deposit their client funds into IOLTA accounts and impoverished Texas citizens still were unable to obtain legal assistance because of a lack of resources. Texas's voluntary IOLTA program yielded only $1 million per year. Following the lead of several other states and the recommendation of the American Bar Association, in 1988, the Texas Supreme Court made

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(footnote continued)

of time. When this determination is made in good faith, then an attorney cannot be liable for this decision. *Id.* § 7.

[5] TEXAS RULES OF COURT – STATE, Rules Governing the Operation of the Texas Equal Access to Justice Program [TEAJF rule] rule 10 (West 1996).

[6] *Id.* rule 15. The TEAJF, however, may provide funds "to finance suits against governmental entities on behalf of individuals in order to secure entitlement to benefits", such as Social Security, Medicaid, and public housing. *Id.*

attorney participation in the IOLTA program mandatory, requiring that attorneys deposit client funds in IOLTA accounts under certain circumstances.[7] The revised rules, which became effective in 1989, state that

> [a]n attorney . . . receiving in the course of the practice of law . . . client funds that are nominal in amount or are reasonably anticipated to be held for a short period of time, *shall* establish and maintain a separate interest-bearing demand account at a financial institution and *shall* deposit in the account all those client funds.[8]

The rules further guide an attorney's decision as to whether funds are suitable for deposit in an IOLTA account, stating that a client's funds may be deposited in an IOLTA account only if

> such funds, considered without regard to funds of other clients which may be held by the attorney . . ., could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the account, service charges, accounting costs and tax reporting costs which would be incurred in

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[7] Attorneys and law firms must open their own IOLTA accounts at a financial institution and direct the depository institution "to remit, at least quarterly, interest earned on the average daily balance in the account, less reasonable service charges" to the TEAJF. TEAJF rules 7, 9.

[8] TEX.GOV'T CODE ANN. tit. 2, subtit. G, app. A, art. 11 § 5 (West Supp.1995) (emphasis added).

attempting to obtain interest on such funds for the client.[9]

Under the mandatory IOLTA program, Texas realized a dramatic increase in IOLTA revenue, with recent earnings of approximately $10 million per year. The TEAJF distributes these funds to various non-profit organizations who apply to the TEAJF for funding.

*Procedural History*

The plaintiffs' objections to the activities of some of the IOLTA fund recipients, such as those groups providing legal aid to refugees seeking political asylum in the United States and those organizations assisting death row inmates to challenge their death sentences, prompted them to bring this suit.[10] The plaintiffs allege that the IOLTA program constitutes an impermissible taking of property, in violation of the Fifth Amendment of the United States Constitution, and that the program also forces them to support speech that they find offensive, in violation of the First Amendment. The plaintiffs request compensation for the interest proceeds that the Texas IOLTA program earned from their deposit and an injunction against the further application of the Texas IOLTA program.

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[9] TEAJF rule 6.

[10] The plaintiffs consist of Michael J. Mazzone, a Texas attorney who regularly places clients' funds into an IOLTA account and who asserts that practical problems prevent him from practicing law without collecting nominal or short-term client funds; William J. Summers, a Texas citizen who has funds currently held in an IOLTA account and who regularly uses Texas attorneys; and the Washington Legal Foundation, a public interest law firm whose members are similarly situated to Mazzone and Summers.

The defendants[11] moved to dismiss the case for failure to state a claim. Though the district court denied this motion, it granted the defendants' subsequent motion for summary judgment and denied the plaintiffs' summary judgment motion. The district court, finding the logic of the First and Eleventh Circuits "compelling",[12] reasoned that there was no property interest at stake in the interest proceeds earned on funds deposited in IOLTA accounts.[13] Having made this determination, the district court then dismissed the plaintiffs' First and Fifth Amendment arguments.[14] The district court concluded by holding that the TEAJF is entitled to Eleventh Amendment immunity against all of the plaintiffs' claims and that Newton is subject only to the plaintiffs' claims of injunctive and prospective relief. The plaintiffs now appeal the district court's decision.

II.

It has been suggested that the IOLTA program represents a successful, modern-day attempt at alchemy.[15] While legends abound concerning the ancient, self-professed alchemists who worked tirelessly towards their goal of changing ordinary metal into precious gold, modern society

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[11] In its suit, the plaintiffs named as defendants the TEAJF; W. Frank Newton, the director of the TEAJF; and all the Justices of the Texas Supreme Court.

[12] *Washington Legal Found. v. Texas Equal Access to Justice Found.*, 873 F.Supp. 1, 6-7 (W.D.Tex.1995) (citing *Washington Legal Found. v. Massachusetts Bar Found.*, 993 F.2d 962, 975-76 (1st Cir.1993) and *Cone v. State Bar of Fla.*, 819 F.2d 1002, 1004 (11th Cir.), *cert. denied*, 484 U.S. 917, 108 S.Ct. 268, 98 L.Ed.2d 225 (1987)).

[13] *Id.* at 7.

[14] *Id.* at 8, 10.

[15] AMERICAN BAR ASS'N, CIVIL JUSTICE: AN AGENDA FOR THE 1990'S 56-72 (1989).

generally scoffs at this attempt to create "something from nothing". The defendants in this case denounce such skepticism, declaring that they have unlocked the magic that eluded the alchemists. The alchemists failed because the necessary ingredients for their magic did not exist in historical times: the combination of attorney's client funds and anomalies in modern banking regulations. According to the defendants' theory, the interest proceeds generated by Texas's IOLTA accounts exist solely because of an anomaly in banking regulations and, until the creation of the IOLTA program, that interest belonged to no one. The defendants then contend that Texas used the IOLTA program to stake a legitimate claim to these funds and that the plaintiffs cannot now seek to repossess the fruits of this magic as their own. We, however, view the IOLTA interest proceeds not as the fruit of alchemy, but as the fruit of the clients' principal deposits.

State law defines "property" and the United States Constitution protects private property from government encroachment.[16] Texas observes the traditional rule that "interest follows principal", which recognizes that interest earned on a deposit of principal belongs to the owner of the principal.[17] In the light of this rule, it seems obvious that the interest earned in the IOLTA accounts is the property of the clients whose money is held in those accounts; nevertheless, the district court adopted the theory espoused by the First and Eleventh Circuits, which circumvents this rule. The district court concluded that the plaintiffs cannot "have a [cognizable] property interest in interest proceeds that, but

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[16] *Webb's Fabulous Pharmacies v. Beckwith,* 449 U.S. 155, 161, 101 S.Ct. 446, 450-51, 66 L.Ed.2d 358 (1980) (citing *Board of Regents v. Roth,* 408 U.S. 564, 577, 92 S.Ct. 2701, 2709, 33 L.Ed.2d 548 (1972)).

[17] *E.g., Sellers v. Harris County,* 483 S.W.2d 242, 243 (Tex.1972).

for the IOLTA Program, would have never been generated".[18] This reasoning, though, does not give proper weight to Supreme Court precedent.

In *Webb's Fabulous Pharmacies v. Beckwith,* the Supreme Court addressed a similar situation.[19] The case arose when the purchase of Webb's Fabulous Pharmacies faltered because, at the closing, the purchaser learned that Webb's had substantial debt that was not previously revealed. The purchaser then filed a complaint of interpleader in Florida state court and tendered the $1.8 million purchase price to the clerk of court. Florida law required the clerk to place the interpleaded funds into an interest-bearing account, to retain the interest earned for the court, and to deduct statutorily-defined fees for maintaining the funds. During the following year while the matter was being resolved, the interpleaded funds earned over $100,000 in interest. The court then appointed a receiver for Webb's, who promptly demanded that the clerk deliver the funds to him. The clerk surrendered the funds, but withheld approximately $10,000 for administrative fees and the $100,000 in interest that had accrued. The creditors then filed suit in state court to recover the interest. Ultimately, the Florida Supreme Court ruled against the creditors, holding that there was no unconstitutional taking because money deposited with the clerk was public money, interest earned on public money was not private property, and the statute only took that which it

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[18] *Washington Legal Found.*, 873 F.Supp. at 7 (citing *Massachusetts Bar Found.*, 993 F.2d at 980; Cone, 819 F.2d at 1005- 07).

[19] 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980).

created.[20] This decision prompted the creditors to appeal to the United States Supreme Court.

The Supreme Court began by noting that the principal deposited with the clerk clearly constituted private property under Florida law.[21] The Court then determined that because the principal was "held only for the ultimate benefit of Webb's creditors, not for the benefit of the court"[22] and eventually would be distributed to them, state law gave the creditors a property interest proportional to their share of the principal.[23]

Having decided the ownership of the principal, the Court turned to the interest on the principal, "the fruit of the fund's use".[24] Reaching the opposite conclusion from that of the Florida Supreme Court,[25] the *Webb's* Court held that simply because the state ordered the placement of interpleaded funds into an interest-bearing account does not mean that the state can assert ownership of that interest.[26] Recognizing that "[t]he usual and general rule [under Florida law] is that any interest on an interpleaded and deposited fund follows the principal and is to be allocated to those who are ultimately to be the owners of that principal", the Court ruled that "earnings of a fund are incidents of ownership of

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[20] *Beckwith v. Webb's Fabulous Pharmacies,* 374 So.2d 951, 952-53 (Fla.1979) (per curiam), *rev'd, Webb's Fabulous Pharmacies v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980).

[21] *Webb's Fabulous Pharmacies,* 449 U.S. at 160, 101 S.Ct. at 450.

[22] *Id.* at 161, 101 S.Ct. at 451.

[23] *Id.*

[24] *Id.* at 162, 101 S.Ct. at 451.

[25] *Beckwith,* 374 So.2d at 953 (finding no unconstitutional taking because the IOLTA program only took the interest that it created).

[26] *Id.* at 162, 101 S.Ct. at 451.

the fund itself and are property just as the fund itself is property."[27] The Court then concluded that the Florida law perpetrated an unconstitutional taking of the interest, which is the property of the creditors who own the principal.[28]

After *Webb's,* numerous state courts debated the constitutionality of IOLTA programs. With the exception of the Indiana Supreme Court,[29] these courts agreed that *Webb's* was inapposite because of the difference in size between the deposit in *Webb's* and the funds eligible for deposit in IOLTA accounts.[30]

In 1987, the Eleventh Circuit considered the IOLTA issue in a suit challenging Florida's version of the IOLTA

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[27] *Id.* at 162-63, 101 S.Ct. at 451-52.

[28] *Id.* at 163, 101 S.Ct. at 451-52.

[29] The Indiana Supreme Court refused to implement an IOLTA program, concluding that the program diverts clients' funds, because the interest proceeds belong to the clients, and convolutes attorneys' fiduciary duty to their clients. *In re Ind. State Bar Ass'ns Petition to Authorize a Program Governing Interest on Lawyers' Trust Accounts,* 550 N.E.2d 311, 312-15 (Ind.1990) (*per curiam*).

[30] *See In re Ark. Bar Ass'n Petition to Authorize a Program Governing Interest on Lawyer's Trust Accounts,* 283 Ark. 252, 675 S.W.2d 355, 357 (1984), modified, 289 Ark. 595, 709 S.W.2d 400 (1986); *Carroll v. State Bar of Cal.,* 166 Cal.App.3d 1193, 213 Cal.Rptr. 305, 312, *cert. denied,* 474 U.S. 848, 106 S.Ct. 142, 88 L.Ed.2d 118 (1985); *In re Interest on Trust Accounts,* 402 So.2d 389, 395-96 (Fla.1981); *Petition by the Mass. Bar Ass'n,* 395 Mass. 1, 478 N.E.2d 715, 718 (1985); *In re Petition of Minn. State Bar Ass'n,* 332 N.W.2d 151, 158 (Minn.1982); *Petition of N.H. Bar Ass'n,* 122 N.H. 971, 453 A.2d 1258, 1261 (1982); *In re Interest on Lawyers' Trust Accounts,* 672 P.2d 406, 408 (Utah 1983). While forty-nine states and the District of Columbia have adopted an IOLTA program in one form or another, *In re Indiana State Bar Ass'n,* 550 N.E.2d at 311, most states adopted the program without opinion or through legislation.

program.[31] The Eleventh Circuit distinguished *Webb's* on the basis that *Webb's* involved the ownership of over $100,000 in accrued interest, an amount that clearly exceeded any fees that were assessed.[32] In contrast, the Florida IOLTA program only concerned deposits that were so small or short-term that the administrative costs of maintaining an interest-bearing NOW account for that deposit would exceed any interest earned.[33] Relying on this factual distinction, the Eleventh Circuit concluded that Florida's IOLTA program does not commit an unconstitutional taking, reasoning that the owner of principal has no legitimate expectation of earning interest on money deposited into a Florida IOLTA account because "the use of [the client's] money had no net value, therefore there could be no property interest for the state to appropriate".[34] According to the Eleventh Circuit, the use of the money had no net value because the IOLTA program only takes the interest from those deposits that do not produce interest in excess of the administrative expenses incurred.[35]

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[31] *Cone,* 819 F.2d at 1002. The Florida IOLTA program was "voluntary", giving its attorneys the option of whether to participate. The clients, however had no choice, other than to choose an attorney who did not use the program. In *Cone,* the plaintiff paid her attorneys $100 to probate her husband's estate. The attorneys failed to return $13.75 of that amount to the plaintiff, which, during the following eleven years, earned $2.25 in interest. The plaintiff's attorneys paid that interest to Florida's IOLTA program and the plaintiff sued to recover that interest.

[32] *Id.* at 1007.

[33] *Id.* at 1006-07.

[34] *Id.* at 1007.

[35] *Id.* The First Circuit, in dicta, reached the same conclusion. *See Massachusetts Bar Found.,* 993 F.2d at 976. In that case, the First Circuit stated that the plaintiffs did not assert property rights in the IOLTA interest proceeds, but sought only to protect the right to exclude the state from the use of their principal. *Id.* at 975-76. The right to exclude is one

(continued...)

Although the Eleventh Circuit explicitly says otherwise,[36] inherent in its *Cone* analysis is the notion that the value of the alleged property involved determines whether there is a cognizable property interest. Under *Cone*, "'property' is [erroneously] redefined as an interest that must necessarily benefit its owner".[37] The *Webb's* decision, however, creates a rule that is independent of the amount or value of interest at issue, holding that a property interest existed in the accrued interest simply because "[t]he earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property".[38] We see no reason why this rule does not apply to the instant case.

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(footnote continued)

of the sticks in the bundle of property rights. *Id.* The Court, nevertheless, held that the interest earned on IOLTA accounts was not the plaintiff's property, *id.* at 976, an issue that was not properly before it. The First Circuit employed reasoning that parallels the decision in *Cone*, concluding that the IOLTA interest belongs to no one. *Id.* at 980.

[36] *Cone*, 819 F.2d at 1007 (stating that the decision does not establish "a de minimis standard for Fifth Amendment takings").

[37] Mary O. Sinibaldi, Note, *The Takings Issue in California's Legal Services Trust Account Program*, 12 HASTINGS CONST.L.Q. 463, 492 (1985).

[38] *Webb's Fabulous Pharmacies*, 449 U.S. at 164, 101 S.Ct. at 452. The *Webb's* Court concluded by holding that the Florida statute appropriated "the value of the use of the fund for the period in which it is held". *Id.; see also* Sinibaldi, *supra* note 37, at 493.

The *Cone* Court was correct to note that the value of the property involved does not effect the determination of whether a property interest exists; indeed, the Supreme Court rejected this position in *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982), in which the Court held that "constitutional protection for the rights of private property cannot be made to depend on the size of the area permanently occupied." *Id.* at 436, 102 S.Ct. at 3176-77 (ruling that an ordinance requiring landlords to allow cable television providers to install small cable boxes on the roofs of their buildings was a permanent physical occupation, thereby entitling the landlords to

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The *Cone* court also failed to consider the precise events of the transaction, concluding that the only protectable property interest in interest proceeds attaches to the amount of interest that remains after a bank deducts its charges from the interest earned, because the owner of the principal only has a legitimate expectation of receiving those interest proceeds.[39] It appears, however, that a bank pays interest on the account and then deducts fees. It is a two-part process. As a result, a property interest attaches the moment that the interest accrues, from which the bank then deducts its charges from the depositor's account. Furthermore, the *Webb's* Court noted that Florida was under no obligation to place the interpleaded funds into an interest-bearing account, but once it did so, then any interest earned belongs to the depositor. The same rule applies to IOLTA accounts. Ethical rules historically demanded that attorneys hold their clients' funds in trust accounts, choosing the type of account in accordance with the best interests of the client. If attorneys still had this latitude, clients could not complain

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(footnote continued)

compensation despite the small area appropriated and the fact that the installation actually enhanced the value of the buildings).

The defendants in the instant case suggest that *Loretto* does not govern IOLTA because money, unlike real property, is fungible and deductions from the IOLTA account are not physical appropriations of property. *Cf. United States v. Sperry Corp.*, 493 U.S. 52, 62 n. 9, 110 S.Ct. 387, 394-95 n. 9, 107 L.Ed.2d 290 (1989) (holding that the government did not perpetrate a taking when it deducted a statutory fee from the plaintiff's award by the Iran-United States Claims Tribunal instead of requiring the plaintiff to pay the fee separately). This argument is inappropriate because this suit does not concern the constitutionality of deductions for the maintenance of the IOLTA accounts, but rather addresses the ownership of the interest generated. *See id. Sperry* merely confirms that the state may charge fees to those who use its services, and may deduct those fees directly from any amount due to the user.

[39] *Cone*, 819 F.2d at 1007.

that a taking occurred when the attorney placed their funds in a non-interest bearing account, because until the interest accrues, the clients have no cognizable property right in the interest.[40] The Texas IOLTA program, however, requires attorneys to place certain client funds into an IOLTA account and then takes the interest that accrues for itself. In such a case, the plain rule is that the interest proceeds, once they have accrued, belong to the owner of the principal.

The defendants additionally argue that finding a property interest in the IOLTA interest overlooks the fact that, for practical banking reasons, the interest earned in trust accounts could never accrue to the clients. This argument ignores one of the critical driving forces of IOLTA: IOLTA programs became possible only with the announcement of Internal Revenue Service ruling 81-209.[41] In this ruling, the I.R.S. agreed that clients would not be taxed on the interest earned on their deposits in IOLTA accounts provided that they had no choice but to participate in the program.[42] By the terms of this ruling, if clients have any control over the interest generated from their nominal and short-term deposits into IOLTA accounts, then the interest generated is taxable income.[43] To prevent this situation, Texas gave itself an

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[40] *See Webb's Fabulous Pharmacies,* 449 U.S. at 161, 101 S.Ct. at 451 ("[A] mere unilateral expectation . . . is not a property interest entitled to protection.")

[41] Rev.Rul. 81-209, 1981-2 C.B. 16; *see also* Rev.Rul. 87-2, 1987-1 C.B. 18 (restating the decision announced in Rev.Rul. 81-209).

[42] Rev.Rul. 81-209, 1981-2 C.B. at 17 (justifying the tax- exempt status of IOLTA interest because under IOLTA plans, "no client may individually elect whether to participate in the program" and "bars clients from receiving the benefit of any interest earned").

[43] The I.R.S. was concerned about IOLTA programs providing a means to assign income and to avoid taxes on that income. By prohibiting clients from having any control over IOLTA funds, the I.R.S. is satisfied that the assignability problem is mooted.

IOLTA monopoly, reserving all the IOLTA interest proceeds for itself and requiring all of its attorneys to participate in the program. If private charities were to establish private IOLTA programs and clients could choose the program to which their funds went, then clients suddenly would have taxable income. Applying the defendants' arguments to such a scenario, the IOLTA funds would be too minimal to return to the clients, therefore falling outside of the *Cone* definition of property, yet clients still would have to pay income tax on the interest earned, interest which *Cone* would say was not their property. This situation flies in the face of reason.

We are also hesitant to declare that such interest is not property lest we incite a new gold rush, encouraging government agencies to dissect banking regulations to discover other anomalies that lead to "unclaimed" interest. One possible source is the interest earned by banks during the float time of checks. Consider a customer who deposits a check drawn on a payor bank with a depositary bank. "In a simple case, where the Federal Reserve Bank is the only intermediary, the depositary bank will present that check to the Fed and receive a [provisional] credit in its reserve account."[44] The Fed then presents the check to the payor bank, whose account is debited and the payor bank must send notice of dishonor within the defined period or be liable for the amount.[45] Typically, this process takes one to two days, during which time the depositary bank has a provisional credit from the Federal Reserve in the amount of the check. Until recently, depositary banks were not required to pay interest to their customers during the time between the

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[44] Robert D. Cooter & Edwin L. Rubin, *Orders and Incentives as Regulatory Methods: The Expedited Funds Availability Act of 1987*, 35 U.C.L.A.L.REV. 1115, 1127 (1988).

[45] *See id.*

deposit of funds and the payor banks' deadline to send the notice of dishonor, effectively giving the depositary banks an interest-free loan on the deposited funds during that time because the depositary banks could treat the provisional credit like cash reserves. This interest-free loan appears very similar to the one that the Texas Supreme Court sought to exploit with the IOLTA program and the interest earned on some checking accounts conceivably could fall below any benefits received, creating an IOLTA-like situation. While depositary banks now must pay interest on deposits from the time that they receive provisional credit from the Fed, credit unions are exempt from this requirement and still receive the benefit of these "interest-free loans".[46]

This is only one example of another "anomaly" in the banking industry and we cannot believe that such anomalies each create funds that belong to nobody. The traditional rule that interest follows principal must apply because that rule compensates the owners of the principal for the use of their funds. If a bank customer chooses, however, to allow the bank to profit in this manner, that decision does not give the state carte blanche to claim that property as its own. As technology continues to advance, the speed with which such transactions can occur will continue to increase, providing greater opportunities for states to try to collect the fractions of pennies that could be earned as interest during the float time of all these activities. Indeed, the faster the funds move, the more and more difficult it will be for individuals to make a practical claim to such funds. Nevertheless, the rule remains the same: any interest that accrues belongs to the owner of the principal, unless they agree otherwise.[47]

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[46] *See* 12 U.S.C.A. § 4005(a), (b) (West 1989).

[47] Furthermore, we also note that under the current IOLTA program, tax law seemingly defines property. If interest was no longer taxed, banks

(continued...)

III.

The district court's decision on the merits is wholly premised on the notion that clients do not have a valid property interest in the interest proceeds earned on funds in IOLTA accounts. Having rejected this premise, we vacate the district court's award of summary judgment to the defendants and denial of summary judgment to the plaintiffs. We remand this case for reconsideration in the light of the principles explained in this decision and for further factual development of the record, such as the clarification of the types of account pooling permitted by the TEAJF rules.

With respect to the merits of the plaintiffs' claims, we note that to prevail on their taking claim, the plaintiffs must demonstrate that the taking was against the will of the property owner.[48] That or a similar showing would also likely be necessary to prevail on their First Amendment claim. We express no opinion as to whether such a showing has been, or can be, made in the context of this case. We leave these and such other issues as may surface to be addressed in the first instance by the district court on remand.

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(footnote continued)

would not have to send 1099s, thereby greatly decreasing the administrative costs of IOLTA accounts. In this case, nearly all deposits would earn interest and clients clearly would be entitled to their funds. We find no basis to hinge property interests on the fickle tax code. Under the current scheme, any change in the costs to banks of managing small deposits would impact the determination of whether a property right in IOLTA interest exists. *See* Kenneth P. Kreider, Note, *Florida's IOLTA Program Does Not "Take" Client Property for Public Use,* 57 U.CIN.L.REV. 369, 391-93 (1988). This short-sighted view of property renders it unacceptable.

[48] *See Yee v. City of Escondido,* 503 U.S. 519, 527, 112 S.Ct. 1522, 1528, 118 L.Ed.2d 153 (1992).

## IV.

Finally, the district court also granted the defendants' request for immunity under the Eleventh Amendment with respect to the plaintiffs' claim for monetary restitution. The parties now only dispute whether the district court erred by declaring the defendants immune to the plaintiffs' restitution claim. The parties do not seriously challenge this portion of the district court's ruling; the defendants concede that they are subject to the plaintiffs' prospective injunction claims and the plaintiffs admit that their "principal concern all along has been in obtaining prospective injunctive relief". We suggest another reason for the parties' lackadaisical approach to this part of the decision: they realize that the district court is correct.

The Eleventh Amendment shields states and their agencies from suits in federal court without the states' consent.[49] Initially, we note that the Texas Supreme Court is entitled to Eleventh Amendment immunity.[50] This immunity extends to the TEAJF because the Texas Supreme Court created the TEAJF pursuant to its rule-making authority and the TEAJF acts on behalf of the Texas Supreme Court to carry out its role, which the Texas Supreme Court defined.[51] Similarly, defendant Newton is entitled to immunity because he is being sued in his official capacity as chairman of the TEAJF, and therefore is also a state actor. The immunity that applies, as held by the district court, is limited and protects the defendants only from the plaintiffs' claims for

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[49] *Word of Faith World Outreach Ctr. Church v. Morales,* 986 F.2d 962, 965 (5th Cir.), *cert. denied,* 510 U.S. 823, 114 S.Ct. 82, 126 L.Ed.2d 50 (1993).

[50] *See Lewis v. Louisiana State Bar Ass'n,* 792 F.2d 493, 497 (5th Cir.1986).

[51] *See id.* at 497 & n. 4.

reimbursement because the Eleventh Amendment does not protect the state from federal suits seeking injunctive relief.[52] Accordingly, we hold that the district court did not err on this issue.

V.

For the foregoing reasons, we find that the district court erred by holding that the clients do not have a cognizable property interest in the interest proceeds that are earned on their deposit in IOLTA accounts. We VACATE the district court's award of summary judgment for the defendants and denial of summary judgment for the plaintiffs and REMAND for further consideration. Finally, we AFFIRM the limited immunity that the district court granted to the defendants.

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[52] *Word of Faith,* 986 F.2d at 965 (5th Cir.); *see also Lewis,* 792 F.2d at 497. The parties also disagree over whether the plaintiffs are entitled to monetary relief under their 42 U.S.C. § 1983 claim for monetary damages. Because neither a state nor state officials sued in their official capacity are "persons" within the meaning of § 1983 when the relief sought is monetary, the plaintiffs cannot recover their claim for reimbursement from the defendants. *See Will v. Michigan Dep't of State Police,* 491 U.S. 58, 69-71 & n. 10, 109 S.Ct. 2304, 2311-12 & n. 10, 105 L.Ed.2d 45 (1989).

UNITED STATES DISTRICT COURT
W.D. TEXAS

AUSTIN DIVISION

Civ. No. A-94-CA-081 JN

WASHINGTON LEGAL FOUNDATION, Michael J. Mazzone, and William R. Summers

v.

TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION, W. Frank Newton, Thomas R. Phillips, Raul A. Gonzalez, Jack Hightower, Nathan L. Hecht, Lloyd Doggett, John Cornyn, Bob Gammage, Craig T. Enoch and Rose Spector.

January 19, 1995

MEMORANDUM ORDER AND JUDGMENT

NOWLIN, District Judge.

Before the Court are the Motion for Summary Judgment filed by Defendant Texas Equal Access to Justice Foundation's ("TEAJF") and Defendant W. Frank Newton, its chair, the Motion for Summary Judgment filed by Defendants Thomas Phillips, Raul Gonzalez, Jack Hightower, Nathan Hecht, Lloyd Doggett, John Cornyn, Bob Gammage, Craig Enoch, and Rose Spector ("the Supreme Court Defendants"),[1] and the Motion for Summary Judgment

[1] The Supreme Court Defendants' Motion for Summary Judgment simply adopts the positions taken by the TEAJF in its Motion for Summary Judgment.

filed by the Plaintiffs, Washington Legal Foundation, William R. Summers, and Michael J. Mazzone. Also before the Court are the Responses addressing these motions, and the Replies addressing these Responses. Having considered these pleadings, the evidence submitted by the parties, the arguments of counsel, and the relevant law, the Court enters the following decision.

*NATURE OF THE CASE*

The Plaintiffs in this action are the Washington Legal Foundation, a self-described non-profit public interest law and policy center, Michael Mazzone, a Texas resident and attorney licensed to practice by the Texas Bar, and William Summers, a Texas resident and consumer of legal services rendered by members of the Texas Bar. The Plaintiffs have filed this action pursuant to 42 U.S.C. § 1983, claiming that the Texas Interest on Lawyers' Trust Accounts ("IOLTA") Program, which is implemented and overseen by the Texas Equal Access to Justice Foundation ("TEAJF"), violates their rights under the First and Fifth Amendments of the United States Constitution. In addition to a declaratory judgment finding the IOLTA Program unconstitutional, the Plaintiffs seek injunctive relief prohibiting mandatory participation in the IOLTA Program, a return of the full amount of interest earned on Plaintiffs' money placed in IOLTA trust accounts, and an award of costs and attorneys' fees.

The Defendants have responded that the IOLTA Program neither effects a taking of the interest generated by the Program in violation of the Fifth Amendment, nor compels speech or involuntary association in violation of the First Amendment. The Defendants alternately contend that the IOLTA Program serves a significant state interest through means narrowly tailored to serve that interest, and, accordingly, there is no First Amendment violation. Finally, the Defendants contend that they are entitled to Eleventh

Amendment immunity and that the TEAJF Defendants are not "persons" subject to suit under 42 U.S.C. § 1983.

*SUMMARY JUDGMENT STANDARD*

Summary judgment is appropriate if the record discloses "that there is no genuine issue of material fact, and the movant is entitled to judgment as a matter of law." Fed.R.Civ.P. 56(c). To determine whether there are genuine fact issues, the court must first consult the applicable law to ascertain what issues are material. *Lavespere v. Niagara Machine & Tool Works,* 910 F.2d 167, 178 (5th Cir.1990), *cert. denied,* 510 U.S. 859, 114 S.Ct. 171, 126 L.Ed.2d 131 (1993), *abrogated on other grounds,Little v. Liquid Air Corp.,* 37 F.3d 1069 (5th Cir.1994). Next, the court must review the evidence on those issues, viewing the facts and inferences in the light most favorable to the nonmoving party. *Id.*

A party seeking summary judgment bears the initial burden of identifying those portions of the pleadings and discovery on file, together with any affidavits, which it believes demonstrate the absence of a genuine issue of material fact. *Celotex Corp. v. Catrett,* 477 U.S. 317, 325, 106 S.Ct. 2548, 2554, 91 L.Ed.2d 265 (1986). Once the movant carries its burden, the burden shifts to the non-movant to show that summary judgment should not be granted. *Id.* at 324-25, 106 S.Ct. at 2553-54. While the Court must review the facts drawing all inferences most favorable to the party opposing the motion, *Reid v. State Farm Mut. Auto. Ins. Co.,* 784 F.2d 577, 578 (5th Cir.1986), that party may not rest upon mere allegations or denials in its pleadings, but must set forth specific facts showing the existence of a genuine issue for trial. *Anderson v. Liberty Lobby, Inc.,* 477 U.S. 242, 256-57, 106 S.Ct. 2505, 2514, 91 L.Ed.2d 202 (1986). Factual controversies are resolved in favor of the nonmoving party, but only when there is an actual controversy, that is, when both parties have submitted

evidence of contradictory facts. *Little*, 37 F.3d at 1075. However, the court does not, in the absence of any proof, assume the nonmoving party could or would prove the necessary facts. *Id.*

*FACTUAL BACKGROUND*

For the most part, the Parties concede that there is no dispute as to any material fact underlying this cause of action. The material facts relating to the operation of the Texas IOLTA Program are set out below.

Article XI of the Rules of the State Bar of Texas establishes the Texas Equal Access to Justice Program (hereinafter "the IOLTA Program"). Under this program, an attorney receiving client funds that are "nominal in amount" or "reasonably anticipated to be held for a short period of time" is required to place the funds in an unsegregated interest-bearing bank account. *See* State Bar Rules Governing Operation of Equal Access to Justice Program Rule 6. More specifically, the only funds eligible for the IOLTA Program are those which

> could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the account, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain interest on such funds for the client. *Id.*

Under the IOLTA rules, when a client tenders a nominal amount of funds, or funds that will be held for only a short term, the lawyer is obligated to first make an initial determination, using his or her good faith judgment, of whether such funds can be deposited into an account that could reasonably be expected to earn an amount of interest sufficient to offset the cost of establishing and maintaining

the account. *Id.* For purposes of the Plaintiffs' claims, it is important to stress that the only funds eligible for deposit in an IOLTA account are those that have no reasonable possibility of legally generating net interest income benefiting the client. Nothing prohibits an attorney from placing funds into a non-IOLTA account, if such funds are capable of generating net interest income to the client.[2]

Interest generated by these IOLTA accounts is to be paid to the Texas Equal Access to Justice Foundation, a non-profit corporation. *Id.,* Rule 9. The Foundation is charged with administering these funds, awarding them as grants to non-profit organizations that have a primary purpose of delivering legal services to low income persons. *Id.* Rules 10-12.[3] As evidenced by the TEAJF's annual reports, the beneficiary organizations provide a wide range of legal services, ranging from providing legal assistance to

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[2] The Plaintiffs contend that there is a genuine issue of material fact regarding whether the Texas IOLTA program permits Texas attorneys to employ the banking practice of sub-accounting as a means of generating net interest on deposited funds, and whether sub-accounting is a practical means of generating net interest for clients who deposit small amounts of money with their attorney. The Court finds that this issue of fact is not material and therefore does not preclude summary judgment. As conceded by the Defendants, any type of account that can earn interest beyond the costs of maintaining such account is beyond the scope of IOLTA's coverage. In other words, if sub-accounting or some other creative (but legal) banking practice or service permits nominal funds to earn net interest, the IOLTA Program and the Texas Bar do not prohibit Texas lawyers from making use of them, even if the result is the placement of these nominal funds in non- IOLTA accounts.

[3] The professed goals of the IOLTA Program – meeting the unmet legal needs of indigent Texans – is indeed laudable. However the Court is conscious of Justice Holmes' warning that "(a) strong public desire to improve the public condition is not enough to warrant achieving the desire by a shorter cut than the constitutional way of paying for the change." *Pennsylvania Coal Co. v. Mahon,* 260 U.S. 393, 416, 43 S.Ct. 158, 160, 67 L.Ed. 322 (1922).

permanent resident aliens seeking naturalization, to documentation for Central American refugees seeking asylum, to legal services to death row inmates, to various AIDS organizations.[4]

Originally, the Texas IOLTA Program was voluntary. However, with only voluntary participation by Texas lawyers, the Program generated insufficient funds to meet the legal needs of indigent Texans. Consequently, in 1988, the Texas Supreme Court entered an order amending the State Bar Rules and converting the voluntary IOLTA program into the mandatory program presently in operation.[5]

*FIFTH AMENDMENT CLAIMS*

The Plaintiffs allege that the IOLTA Program violates their Fifth Amendment rights by taking their property without just compensation. More specifically, the Plaintiffs

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[4] One of the Plaintiffs' principal objections to the IOLTA Program is that some of the recipient organizations advocate positions to which the Plaintiffs are politically or ideologically opposed, such as expanding the rights of undocumented aliens or broadening the scope of anti-discrimination causes of action. In this regard, it bears noting that the IOLTA Rules prohibit the granting of funds to finance class actions, lawsuits against government entities (except to secure entitlements), or lobbying. *See* IOLTA Rule 15. However, the TEAJF apparently exercises little if any control or administrative influence over the out-of-court self-promotions and solicitations of some vocal attorneys or representatives of the donee entities.

[5] The need for the provision of legal services to low income persons, and possibly for a mandatory *pro bono publico* program for lawyers, have been prominent issues recently facing both the Texas Bar and the Texas Supreme Court. *See, e.g., State Bar of Texas, et al. v. Maria Gomez, et al.,* 891 S.W.2d 243 (Tex.1994). The Court surmises that the well-documented failures of the Texas Bar to meet the legal needs of needy Texans through voluntary activities, as well as the clamor for mandatory *pro bono* by some sectors of the Texas Bar have played a significant role in the implementation of the mandatory IOLTA Program presently under consideration.

allege both 1) that the Program effects a taking of the interest generated by the funds deposited into pooled IOLTA accounts, and 2) that the Program effects a taking of the "beneficial use" of their property by compelling them to deposit their funds in IOLTA accounts to generate income to support the Program.

The Fifth Amendment provides that private property shall not be taken for public use without just compensation. *U.S. Const. amend. V.*[6] For there to be a "taking" within the purview of the Fifth Amendment, the government must interfere "with interests that (are) sufficiently bound up with the reasonable expectations" of the plaintiff asserting the deprivation. *Penn Central Transp. Co. v. New York City,* 438 U.S. 104, 125, 98 S.Ct. 2646, 2659, 57 L.Ed.2d 631 (1978); *see also Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. at 161, 101 S.Ct. at 450 ("[A] mere unilateral expectation or an abstract need is not a property entitled to protection."). In other words, the Plaintiffs must be able to assert a cognizable property interest to raise a Fifth Amendment takings claim. *Ruckelshaus v. Monsanto,* 467 U.S. 986, 1001, 104 S.Ct. 2862, 2871, 81 L.Ed.2d 815 (1984). Whether such an interest exists is a question of state law. *See, e.g., Webb's,* 449 U.S. at 161, 101 S.Ct. at 450 ("[P]roperty interests . . . are not created by the Constitution. Rather they are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law. . . .") (quoting *Board of Regents v. Roth,* 408 U.S. 564, 577, 92 S.Ct. 2701, 2709, 33 L.Ed.2d 548 (1972)).

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[6] This prohibition is made applicable to the states by the Fourteenth Amendment. *Webb's Fabulous Pharmacy, Inc. v. Beckwith,* 449 U.S. 155, 160, 101 S.Ct. 446, 450, 66 L.Ed.2d 358 (1980).

*Ownership of IOLTA-Derived Interest*

Whether the Plaintiffs' can prevail on their Fifth Amendment claim depends in large part upon the characterization and ownership of the interest generated by the funds deposited in the IOLTA accounts – that is, whether they have a cognizable property interest in the IOLTA account interest. There is, of course, no dispute that the nominal funds given by Plaintiff Summers (the client) to Plaintiff Mazzone (his attorney), and which are deposited in Mazzone's IOLTA account, are at all times the property of Summers. The critical issue is to whom the proceeds (*i.e.*, the interest earned) from such funds belong.[7]

The Plaintiffs contend that the client possesses property rights in the interest derived from IOLTA accounts. In support of this proposition, the Plaintiffs rely primarily upon the Supreme Court's decision in *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* 449 U.S. 155, 101 S.Ct. 446, 66 L.Ed.2d 358 (1980). *Webb's* involved a challenge to Florida statute which permitted a county to take as its own the interest accruing on an interpleader fund deposited in the registry of a county court. The interpleaded funds involved in *Webb's* generated interest in excess of $100,000.00 The Supreme Court struck down the statute, holding that the earnings of interpleaded funds are incidents of ownership of the funds itself and are property in the Fifth Amendment context just as the interpleaded fund itself is property. *Webb's,* 449 U.S. at 160-65, 101 S.Ct. at 450-52. The rationale for the *Webb's* decision was based upon the "usual and general rule (that) any interest on an interpleaded and deposited fund follows the principal and is to be allocated to

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[7] For purposes of this inquiry, it must at all times be kept in mind that, under the IOLTA Rules, the principal amounts at issue cannot be reasonably be expected to earn net interest on their own.

those who are ultimately to be the owners of that principal." 449 U.S. at 162, 101 S.Ct. at 451. On the basis of this holding, the Plaintiffs claim that they have a property interest in the interest earned on their nominal or short-term IOLTA funds.[8]

The principles enunciated in *Webb's* have been frequently invoked in challenges to IOLTA programs operating in other jurisdictions. Such invocations have been almost uniformly without success.[9]

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[8] The Plaintiffs point out that the Supreme Court cited as an example of this "usual and general rule" *Sellers v. Harris County,* 483 S.W.2d 242 (Tex.1972), a decision of the Texas Supreme Court involving essentially the same operative facts as *Webb's.* In *Sellers,* the Texas Supreme Court ruled that the interest generated from $1,000,000 in insurance policy proceeds that were interpleaded into a county court's registry belonged to the owner of the principal and not the county, which claimed it was entitled to the interest pursuant to state statute. These proceeds generated interest in excess of $6,000.00 per month. *Sellers,* 483 S.W.2d at 242.

[9] The supreme courts of all fifty states have examined the constitutionality, efficacy, and propriety of IOLTA programs. Forty-nine of these state courts have approved them in one form or another. The lone exception is the Indiana Supreme Court, which declined to adopt the state bar's proposed IOLTA program in a nonadversarial proceeding. *See In re Indiana State Bar Association's Petition to Authorize a Program Governing Interest on Lawyer's Trust Accounts,* 550 N.E.2d 311 (Ind.1990). However, contrary to the Plaintiffs' characterization of this opinion, the Indiana Supreme Court's refusal to adopt an IOLTA program was *not* predicated on constitutional grounds, but rather solely upon the court's view that the proposed IOLTA program was contrary to its interpretation of the ethical obligations of Indiana attorneys. *See Id.* at 315 ("[L]et there be no question that the IOLTA program currently promoted by the Indiana Bar Association violates our Rules for the Discipline of Attorney and Rules of Professional Conduct."). This Court declines to consider the ethical implications of the Texas IOLTA Program as such questions are more properly raised before the entity charged with regulating the conduct of members of the Texas Bar--namely, the Texas Supreme Court. *See* TEX.GOV.CODE ANN. § 81.011(c) (Vernon 1988).

In *Cone v. State Bar of Florida,* 819 F.2d 1002, 1004 (11th Cir.), *cert. denied* 484 U.S. 917, 108 S.Ct. 268, 98 L.Ed.2d 225 (1987), the Eleventh Circuit evaluated the applicability of the holding in *Webb's* to a Fifth Amendment challenge to the Florida Bar's Interest on Trust Accounts ("IOTA") program.[10] The Eleventh Circuit found that, despite "superficial similarities," the *Webb's* decision had no application in the IOTA context, due to the fact that the use of funds in an IOTA account had no net value. *Cone,* 819 F.2d at 1007. As the circumstances surrounding the funds and related banking practices could not lead to a legitimate expectation of interest exclusive of administrative costs and expenses, there could be no property interest for the state to appropriate via the collection of interest earned on pooled IOTA funds. *Id.* The court stated that there was no taking of property because, standing alone, the plaintiff's funds deposited in her attorney's IOTA (IOTA) account could not earn anything, and consequently, there could be no legitimate claim of entitlement. *Id.*

The holding and reasoning in *Cone* was cited with approval by the First Circuit in *Washington Legal Foundation v. Massachusetts Bar Foundation,* 993 F.2d 962, 975-76 (1st Cir.1993), a case involving another unsuccessful challenge to the Massachusetts Bar's IOLTA Program. The court also noted some "superficial similarities" between *Webb's* and the challenge to Massachusetts IOLTA program, but stressed a fundamental difference – namely, that the claimants in *Webb's* had property rights in the accrued net interest generated by the deposited funds, while in the IOLTA context, the property interests are essentially intangible. *Id.* In accordance with the decision in *Cone,* the

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[10] The Florida Bar's Interest On Trust Accounts program is similar in both purpose and operation to the Texas IOLTA program. *See Cone,* 819 F.2d at 1003.

First Circuit held that the Plaintiffs' claimed property rights in both the interest generated by their funds and the beneficial use of the funds deposited in IOLTA accounts were insufficient to support a Fifth Amendment claim.

The logic supporting both of these opinions is compelling. By definition, the only funds eligible for deposit in an IOLTA account are those which are incapable of earning net interest if deposited by themselves in an individual (non-pooled) account. Further, as stated above, for there to be a "taking" within the purview of the Fifth Amendment, the state action must interfere with interests that are sufficiently bound up with the reasonable expectations of the person asserting the deprivation. This "reasonable expectation" of a property interest is foreclosed by the very wording and operation of the rules governing the IOLTA program – that is, if there is any reasonable expectation of realizing net interest on a sum, the sum is exempted from IOLTA coverage. Simply put, the Court cannot conclude that the Plaintiff's have a property interest in interest proceeds that, but for the IOLTA Program, would never have been generated. Without such a property interest, the Plaintiffs are unable to state a viable Fifth Amendment claim pertaining to their ownership of the interest generated by funds placed in IOLTA accounts.

The Court finds that in the case of the Texas IOLTA Program (as in the case of the Florida and Massachusetts programs), it is only through combining small or short-term deposits that there is a possibility of creating interest. Put another way: such interest has been generated only by virtue of "an anomaly created by the practicalities of accounting, banking practices, and the ethical obligations of lawyers." *Washington Legal Foundation,* 993 F.2d at 980. It follows then that such interest income is not within the legitimate expectations of the owner of any one of the principal amounts. Accordingly, such amounts cannot be deemed to

be appropriated by the IOLTA program.[11] In sum, the property rights of the Plaintiffs in this action and the claimants in *Webb's* are clearly different, and, as there is no property interest or expectation appropriated, there is no taking for Fifth Amendment purposes. Accordingly, the Court finds that the Plaintiffs have failed to allege a cognizable Fifth Amendment takings claim with regard to the interest generated by funds placed in IOLTA accounts.

The Plaintiffs cite two additional cases involving prison inmates as authority for the proposition that the client has a protectable property interest in the proceeds generated from funds deposited into an IOLTA account. In *Tellis v. Godinez,* 5 F.3d 1314 (9th Cir.1993), *cert. denied* 513 U.S. 945, 115 S.Ct. 354, 130 L.Ed.2d 309 (1994) a prisoner brought suit against prison officials alleging that they violated his due process rights by withholding interest earned on funds in his personal bank account. The Ninth Circuit recognized that the prisoner did indeed have a property right in the interest generated by his funds. However, the Ninth Circuit's holding must be read in the context of the relevant statute upon which the prisoner's claim was based. This statute provided that the interest and income earned on the money in the prisoner's trust fund must be credited to that fund *after* applicable charges were deducted. *Tellis,* 5 F.3d at 1316 (quoting Nev.Rev.Stat. § 209.241). Contrary to the Plaintiffs' argument, *Tellis* simply cannot be read as supporting the broader conclusion that a person has a protected property interest in interest generated from his or her funds, regardless of whether any net interest can ever be realized.

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[11] *See Cone,* 819 F.2d at 1007: "IOLTA programs do not amount to a taking because they create interest which was not within the reasonable expectations of any one of the principal amounts."

The Plaintiffs also cite the Fifth Circuit's opinion in *Eubanks v. McCotter,* 802 F.2d 790 (5th Cir.1986), another case in which prisoners sued prison officials alleging that their failure to pay the prisoners the interest generated by pooled inmate trust funds constituted a taking. The Fifth Circuit reversed the lower court, which had dismissed *sua sponte* the claim as frivolous. The Fifth Circuit found that the prisoners' claims were "not wholly insubstantial or frivolous" and were "minimally sufficient to require a decision on the merits." *Eubanks,* 802 F.2d at 793-94. This, however, is the limit of the extent to which the Fifth Circuit recognized or endorsed the viability of these claims. *See Id.,* at 794. Thus, *Eubanks* applicability to the Plaintiffs' position is tenuous at best.

In scrutinizing the holdings and the underlying facts of both *Tellis* and *Eubanks,* it may be concluded that the prisoners were recognized to have property interests in the interest generated by their inmate trust accounts, but only after applicable charges were deducted. Accordingly, the Court finds that these cases, like *Webb's* and *Sellers* are inapposite.

*Fifth Amendment Protection of*
*Plaintiffs' Expectation Interest*

The Plaintiffs alternately argue that, even if they lack a protected property interest in the generated interest, they have a protected property right to exclude others from the beneficial use of their funds while they are deposited in IOLTA accounts. In support of this purported right, the Plaintiffs rely primarily upon cases standing for the proposition that property owners may exclude others from their real, or tangible property. *See, e.g., Dolan v. City of Tigard,* 512 U.S. 374, 114 S.Ct. 2309, 129 L.Ed.2d 304 (1994) (government requirement that property owner dedicate portion of property within flood plain for public improvements contrary to Fifth Amendment); *Loretto v.*

*Teleprompter Manhattan CATV Corp.*, 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982) (government regulation requiring private property owners to allow conduits for cable television to be attached even when property owners were not cable subscribers was an unconstitutional taking without just compensation); *Kaiser Aetna v. United States,* 444 U.S. 164, 100 S.Ct. 383, 62 L.Ed.2d 332 (1979) (federal government's imposition of a navigational servitude on owners of a private marina requiring that they allow a right of access to the public amounted to an unconstitutional taking). But, as noted, these cases all involve governmental intrusions or interference with real or tangible property. These cases do not recognize a similarly protected property right to control or exclude others from intangible property, and therefore are insufficient to support a finding that the Plaintiffs have a protectable property interest in the beneficial use of IOLTA-eligible funds.[12]

The Plaintiffs do correctly note that there are certain "intangible rights" that merit Fifth Amendment protection. *See, e.g., Lynch v. United States,* 292 U.S. 571, 54 S.Ct. 840, 78 L.Ed. 1434 (1934) (valid contracts are property which cannot be taken without just compensation); *James v. Campbell,* 104 U.S. 356, 26 L.Ed. 786 (1881) (patents entitled to Fifth Amendment protection). However, inherent in these types of property is the necessity of excluding others to preserve the property interest. Accordingly, these cases fail to support the Plaintiffs' proffered analogy. *See Washington Legal Foundation,* 993 F.2d at 974 n. 10 ("[W]e do not finds analogous, intangible property rights which, by their nature or by agreement, require the exclusion of others to preserve the property interest).

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[12] *See Washington Legal Foundation,* 993 F.2d at 974.

To preclude summary judgment on the Plaintiffs' Fifth Amendment claims, the Court would have to find a genuine issue of material fact as to the operation of the IOLTA Program, the nature of the Plaintiffs property interest in interest generated by funds placed in IOLTA accounts, or the effect of the IOLTA Program on the generated interest. The Court finds that there is no factual dispute as to these issues, but only as to the characterizations of the client's property interests, all questions of law. Having resolved these questions in favor of the Defendants, the Court finds that the Plaintiffs' Fifth Amendment claims should be dismissed.[13]

*PLAINTIFFS' FIRST AMENDMENT CLAIMS*

The Plaintiffs further claim that the collection and use of interest generated from funds clients place with their attorneys under the Texas IOLTA Program deprive the clients of their rights of freedom of speech and association guaranteed by the First Amendment.[14]

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[13] The conclusion that the Texas IOLTA Program does not violate the Fifth Amendment is consistent with the holdings of numerous other decisions from other jurisdictions. *See, e.g., Cone, supra; Washington Legal Foundation, supra; In re Interest on Trust Accounts,* 402 So.2d 389 (Fla.1981); *Petition of Minnesota State Bar Association,* 332 N.W.2d 151 (Minn.1982); *Petition of New Hampshire Bar Association,* 122 N.H. 971, 453 A.2d 1258 (1982); *In re Interest on Lawyers Trust Accounts,* 672 P.2d 406 (Utah 1983); *In re Interest on Lawyers Trust Accounts,* 283 Ark. 252, 675 S.W.2d 355 (1984); *Petition of Massachusetts Bar Ass'n,* 395 Mass. 1, 478 N.E.2d 715 (1985); *Carroll v. State Bar of California,* 166 Cal.App.3d 1193, 213 Cal.Rptr. 305 (4th Dist.), *cert. denied sub nom. Chapman v. State Bar of California,* 474 U.S. 848, 106 S.Ct. 142, 88 L.Ed.2d 118 (1985).

[14] The First Amendment provides: "Congress shall make no law respecting an establishment of religion, or prohibiting the free exercise thereof; or abridging the freedom of speech, or of the press; or the right of the people to peaceably assemble, and to petition the Government for a redress of grievances." *U.S. Const. amend. I.* The Fourteenth

(continued...)

"It is well-established that the freedom of speech protected by the First Amendment includes the freedom to choose 'both what to say and what *not* to say.'" *Hays County Guardian v. Supple,* 969 F.2d 111, 123 (5th Cir.1992), *cert. denied* 506 U.S. 1087, 113 S.Ct. 1067, 122 L.Ed.2d 371 (1993) (quoting *Riley v. National Federation for the Blind,* 487 U.S. 781, 797, 108 S.Ct. 2667, 2677, 101 L.Ed.2d 669 (1988)) (emphasis in original). The right to refrain from speech is violated when the government compels an individual to endorse a belief that he or she finds repugnant. *Id.* (citations omitted). It also may be violated when the government compels an individual to subsidize political and ideological purposes with which he or she disagrees. *Id.* (citing *Lyng v. Int'l Union, United Auto Workers,* 485 U.S. 360, 369, 108 S.Ct. 1184, 1191, 99 L.Ed.2d 380 (1988)); *Chicago Teachers Union Local No. 1 v. Hudson,* 475 U.S. 292, 301, 106 S.Ct. 1066, 1073, 89 L.Ed.2d 232 (1986); *Abood v. Detroit Bd. of Educ.,* 431 U.S. 209, 234-35, 97 S.Ct. 1782, 1799, 52 L.Ed.2d 261 (1977).

Essentially, the Plaintiffs claim that their mandatory participation in the IOLTA Program forces clients to financially support, and thereby associate with, various recipient organizations whose purported objectives the Plaintiffs find objectionable.[15] However, at least as far as the

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(footnote continued)

Amendment makes this limitation applicable to the States and to its subdivisions. *See Gitlow v. New York,* 268 U.S. 652, 45 S.Ct. 625, 69 L.Ed. 1138 (1925) and *Lovell v. Griffin,* 303 U.S. 444, 58 S.Ct. 666, 82 L.Ed. 949 (1938).

[15] As noted *supra,* IOLTA Rules prohibit recipient organizations from using grants to fund lobbying or certain types of litigation. These limitations do not lead the Court to conclude that First Amendment issues have not been raised, despite the Defendants' contentions. Admittedly the collection and disbursement of funds appears to lack a First Amendment dimension. However, it is not disputed that the funds (continued...)

client is concerned, such a claim is necessarily predicated upon the Plaintiffs' claim that the funds generated from the IOLTA accounts are, in fact, the property of the client. As determined in the preceding discussion regarding the Plaintiffs Fifth Amendment claims, the interest generated by the IOLTA program is not the property of any of the Plaintiffs, thus, the collection and use of the interest by the IOLTA program does not constitute financial support by the Plaintiffs of the recipient organizations.

Furthermore, the IOLTA Program in no way compels any of the Plaintiffs to actually associate or otherwise be linked with the recipient organizations that they find repugnant (*e.g.*, by becoming members or being publicly listed as benefactors). Because the Plaintiffs have failed to adequately allege any connection between themselves and the IOLTA recipient organizations, the Court finds that the Texas IOLTA Program does not unconstitutionally burden the Plaintiffs' First Amendment rights. *See Washington Legal Foundation,* 993 F.2d at 980. *Compare Carroll v. Blinken,* 957 F.2d 991 (2d Cir.), *cert. denied,* 506 U.S. 906, 113 S.Ct. 300, 121 L.Ed.2d 224 (1992) (compulsory student fees used to support statewide student advocacy organization, which automatically made all students members, impermissibly forced association in violation of the First Amendment).

The Plaintiffs also appear to contend that, even absent any financial link to the IOLTA Program, the mandatory

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(footnote continued)

collected through IOLTA are awarded to meet the otherwise unmet needs for legal service of indigent Texans. The Supreme Court has recognized the expressive nature of litigation within the context of the First Amendment. *See Lehnert v. Ferris Faculty Ass'n,* 500 U.S. 507, 111 S.Ct. 1950, 114 L.Ed.2d 572 (1991). Accordingly, the Court finds that there is expressive activity sufficient to invoke the First Amendment.

Program forces attorneys to be associated with the TEAJF and its recipient organizations. It arguably could be said that the mandatory IOLTA Program forces attorneys to associate with these groups (albeit in an attenuated fashion). However, even if this were true, such compelled association does not give rise to a constitutional violation. In *Keller v. State Bar of California,* 496 U.S. 1, 110 S.Ct. 2228, 110 L.Ed.2d 1 (1990), the Supreme Court considered a challenge brought by California attorneys regarding the use of the state bar's dues to finance certain ideological or political activities. The Court held that the bar's use of compulsory dues to finance activities having "political or ideological coloration" violated the First Amendment, *except* when such expenditures were reasonably or necessarily incurred for the purpose of regulating the legal profession or improving the quality of legal services available to the people of the state. *Keller,* 496 U.S. at 14, 110 S.Ct. at 2236; *see also Lathrop v. Donohue,* 367 U.S. 820, 843, 81 S.Ct. 1826, 1838, 6 L.Ed.2d 1191 (1961). The undisputed purpose of the IOLTA Program is to provide funding for legal services to a substantial segment of the population of Texas. This squarely fits within the purview of improving the quality of the legal service available to the people of the state as contemplated by *Keller.* Furthermore, the extent of an attorney's involvement with the IOLTA Program is merely handling his client's funds in a slightly different fashion than he would otherwise. There is no contribution of the attorney's own funds or his or her bar dues. Accordingly, the Court finds no constitutional infirmity with respect to attorneys' mandatory participation in the IOLTA Program.

Because the Court does not find that the IOLTA Program adversely impacts the Plaintiffs' rights either under the First or Fifth Amendment, the Court will not delve into extended First Amendment analysis regarding whether the Program is adequately tailored to serve the state's claimed interest. It suffices to say that providing indigent Texans

with the means to gain access to the legal system is a significant state interest and the operation of the system imposes minimal burdens upon First Amendment rights of attorneys and their clients. *See, generally, Hays County Guardian v. Supple,* 969 F.2d at 122-24.

*ELEVENTH AMENDMENT AND*
*42 U.S.C. § 1983 IMMUNITY*

The Defendants also argue that they are entitled to Eleventh Amendment immunity and that they are not "persons" for purposes of *42 U.S.C. § 1983.*

*Eleventh Amendment Immunity*

The Eleventh Amendment generally divests federal courts of jurisdiction to entertain suits directed against states. *Green v. State Bar of Texas*, 27 F.3d 1083, 1087 (5th Cir.1994) (citing *Port Auth. Trans-Hudson Corp. v. Feeney*, 495 U.S. 299, 304, 110 S.Ct. 1868, 1971, 109 L.Ed.2d 264 (1990)). Unless consent is given, the Eleventh Amendment forbids suit against a state, a state agency or department of the state by citizens of the state. *Pennhurst State School & Hosp. v. Halderman*, 465 U.S. 89, 100, 104 S.Ct. 900, 907, 79 L.Ed.2d 67 (1984). Suit is barred against a state entity regardless of whether money damages or injunctive relief is sought. *Clark v. Tarrant County, Texas*, 798 F.2d 736, 743 (5th Cir.1986); *Krempp v. Dobbs*, 775 F.2d 1319, 1321 (5th Cir.1985); *Cory v. White*, 457 U.S. 85, 102 S.Ct. 2325, 72 L.Ed.2d 694 (1982).

In a suit challenging a rule of a state supreme court, the supreme court is the real party in interest if it has the ultimate authority to adopt and enforce the rule in question. *Lewis v. Louisiana State Bar Ass'n,* 792 F.2d 493, 497 (5th Cir.1986). In such an instance, moreover, an entity whose role is completely defined by the state supreme court, which acts as the agent of the court, occupies the position of a public agency for purposes of Eleventh Amendment analysis.

*See Lewis v. Louisiana State Bar Ass'n,* 792 F.2d 493 (5th Cir.1986) (Louisiana Supreme Court and state bar association both entitled to Eleventh Amendment immunity from action by unsuccessful bar applicant's due process complaint); *accord Krempp v. Dobbs,* 775 F.2d at 1321. (Suit against Texas State Bar and State Commission on Judicial Conduct barred by Eleventh Amendment).

As noted above, the TEAJF was created by an order of the Texas Supreme Court in 1988, pursuant to the court's inherent power to regulate the practice of law in Texas. Pursuant to that order, the TEAJF has statewide authority to act and carries out its objectives on a statewide basis. Consistent with the logic of *Lewis,* the Court finds that the TEAJF is an arm of the Texas Supreme Court, and consequently the State of Texas, thereby entitling the TEAJF to Eleventh Amendment protection from all of the Plaintiffs' claims.

However, the Eleventh Amendment does not bar suits for injunctive relief against state officials. *Word of Faith World Outreach Ctr. v. Morales,* 986 F.2d 962, 965 (5th Cir.), *cert. denied,* 510 U.S. 823, 114 S.Ct. 82, 126 L.Ed.2d 50 (1993); *Ex Parte Young,* 209 U.S. 123, 28 S.Ct. 441, 52 L.Ed. 714 (1908). Accordingly, to the extent that the Plaintiffs' complaint seeks injunctive relief against the Chairman of the TEAJF, such claims are permitted under the Eleventh Amendment.

*42 U.S.C. § 1983*

A state official acting in his official capacity is not a person under *§ 1983* unless the relief requested in a suit against him in this capacity is prospective relief. *John G. and Marie Stella Kenedy Mem. Found. v. Mauro,* 21 F.3d 667, 671 (5th Cir.), *cert. denied,* 513 U.S. 1016, 115 S.Ct. 577, 130 L.Ed.2d 493 (1994); *Will v. Michigan Dep't of State Police,* 491 U.S. 58, 71 & n. 10, 109 S.Ct. 2304, 2312 & n. 10, 105 L.Ed.2d 45 (1989). Accordingly, to the extent the

Plaintiffs seek prospective relief against the Chairman of the TEAJF, Dean Frank Newton, such claims may proceed; however, any monetary relief is barred.[16]

*CONCLUSION*

The Court declines to address the expressed social, political or public policy concerns related to the current operational procedures of the Texas Equal Access to Justice Foundation as it administers the IOLTA Program. Alleviation of these concerns rests with Texas attorneys and their relationship to the state bar, as well as the care of all Texas voters in the selection of their elected public officials.

Based upon the foregoing analysis, the Court finds that the Defendants' Motions for Summary Judgment should be granted, and the Plaintiffs' claims should be dismissed in their entirety. Further, the Court finds that the Plaintiffs' Motion for Summary Judgment should be denied.

**THEREFORE, IT IS ORDERED** that the Motion for Summary Judgment, filed by the Texas Equal Access to Justice Foundation on December 6, 1994, is hereby **GRANTED.**

**FURTHER, IT IS ORDERED** that the Motion for Summary Judgment, filed by the Supreme Court Defendants on December 6, 1994, is hereby **GRANTED.**

**FURTHER IT IS ORDERED** that the Motion for Summary Judgment, filed by the Plaintiffs on December 8, 1994 is hereby **DENIED.**

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[16] The parties do not address whether the individual justices of the Texas Supreme Court are entitled to Eleventh Amendment Immunity or are persons for *§ 1983* purposes. However, the Court finds that were these issues before it, the same analysis would apply – *i.e.*, the Plaintiffs claims for injunctive remedies may be sought against the individual Justices.

**ACCORDINGLY, IT IS ORDERED, ADJUDGED AND DECREED** that any and all claims brought by the Plaintiffs against the Defendants in the above-numbered and styled cause of action are hereby **DISMISSED WITH PREJUDICE.**

FURTHER, IT IS ORDERED, ADJUDGED AND DECREED that the above-numbered and styled cause of action is hereby DISMISSED WITH PREJUDICE.

**FINALLY, IT IS ORDERED** that Clerk shall **TERMINATE AS MOOT** any motions that remain pending in this action.

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 00-50139

WASHINGTON LEGAL FOUNDATION, William R. Summers, and Michael J. Mazzone,

Plaintiffs-Appellants,

v.

TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; Richard Tate, Chairman, Texas Equal Access to Justice Foundation, Thomas R. Phillips, Chief Justice, and Justices Nathan R. Hecht, Craig T. Enoch, Priscilla R. Owens, James A. Baker, Deborah G. Hankinson, Harriet O'Neill, and Xavier Rodriguez in their official capacities as Justices of the Supreme Court of Texas,

Defendants-Appellees.

Appeal from the United States District Court
for the Western District of Texas, Austin Division

May 31, 2002

ON PETITION FOR REHEARING EN BANC

(Opinion October 19, 2001, 5 Cir., 2001 270 F.3d 180)

Before WIENER, BARKSDALE, and EMILIO M. GARZA, Circuit Judges.

PER CURIAM:

Treating the Petition for Rehearing En Banc as a Petition for Panel Rehearing, the Petition for Panel Rehearing is DENIED. The court having been polled at the request of one of the members of the court and a majority of the judges who are in regular active service not having voted in favor (Fed. R. App. P. and 5th Cir. R. 35), the Petition for Rehearing En Banc is DENIED.

Judge Higginbotham did not participate.

CHIEF JUDGE KING and JUDGES JOLLY, WIENER, BENAVIDES, STEWART, PARKER, and DENNIS, Circuit Judges, dissenting from denial of rehearing en banc.[17]

In this second round of the captioned case, a divided panel of our court reversed the district court's ruling and held the Texas Interest on Lawyers' Trust Accounts (IOLTA) program unconstitutional. Soon afterwards, the Ninth Circuit, sitting en banc, upheld the constitutionality of an essentially identical IOLTA program in the State of Washington.[18] In so doing, the court formulated answers to constitutional questions that are common to both cases, answers that are consistent with those in our district court's

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[17] Judge Higginbotham recused himself from the case, leaving fourteen active Circuit Judges, seven of whom voted for en banc rehearing and seven of whom voted against it. Pursuant to Fifth Circuit operating procedure, an evenly divided vote on an en banc poll results in denial of rehearing en banc, leaving the panel opinion in effect.

[18] *Washington Legal Foundation v. Legal Foundation of Washington*, 271 F.3d 835 (9th Cir. 2001) (holding that, although interest in IOLTA accounts is property, no taking occurred and no just compensation was due).

ruling and Judge Wiener's panel dissent, and thus contrary to those of our panel majority. Despite this split in the circuits, our 2-1 reversal of the district court, and the far-reaching, exceptionally important constitutional and practical consequences of the Fifth Amendment jurisprudence thus established for this circuit by but two of our judges, a tie among voting active judges prevented this case from receiving the rehearing en banc that it so richly deserves. Given (1) the disagreement between our panel majority and the Ninth Circuit sitting en banc, (2) the fact that our panel majority opinion forges novel and far-reaching Takings jurisprudence for this circuit, (3) the inability of the plaintiffs to show any compensable loss whatsoever, and (4) the effect on IOLTA programs that will likely result from the opinion of the panel majority, we find it difficult to understand how any judge of this court (even those who served on this panel) could fail to deem this case worthy of en banc reconsideration, irrespective of what the reasoning and result should be. We are therefore constrained to dissent respectfully from this denial of a rehearing en banc. Our hope is that the Supreme Court will see fit to address this very important case once again and resolve the questions left unanswered by its prior opinion.[19]

WIENER, Circuit Judge, supplementing the foregoing dissent from denial of rehearing en banc:[****]

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[19] *Phillips v. Washington Legal Foundation*, 524 U.S. 156, 172 (Rehnquist, C.J.):

> We express no view as to whether these funds have been "taken" by the State; nor do we express an opinion as to the amount of "just compensation," if any, due respondents. We leave these issues to be addressed on remand.

[****] Chief Judge King and Judges Benavides, Stewart, Parker, and Dennis join in this supplemental dissent.

My reasons for believing that this case is worthy of en banc review are the same as those set forth in the foregoing dissent by the seven of us who voted to rehear it. I now write separately to add the substantive law reasons why I am convinced that we should have reheard this appeal en banc and reinstated the judgment of the district court.

As a practical outcome for our circuit, the panel majority's holding dismantles IOLTA programs that have found favor in all fifty states as a means of funding legal services for the underprivileged while fulfilling lawyers' ethical obligations to contribute to the delivery of such services for that segment of society.[1] Jurisprudentially, the opinion of the panel majority forges novel Fifth Amendment Takings jurisprudence for our circuit by mandating a simple analytical approach – and its scope – that must be taken when courts of this circuit consider a Takings Clause issue. I shall do my best to demonstrate why I believe that the panel majority's reasoning and judgment are wrong.

## I. *IOLTA I*

Following our first go-around with *Washington Legal Foundation v. Texas Equal Access to Justice*,[2] a five-justice majority of the Supreme Court deliberately answered but one

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[1] *Phillips v. Washington Legal Foundation*, 524 U.S. 156, 159 n.1 (1998); Model Rules of Professional Conduct Rule 6.1; State Bar of Tex. Pro Bono Policy; Geoffrey C. Hazard, Jr., After Professional Virtue, 6 Sup. Ct. Rev. 213, 215 (1989).

[2] *Washington Legal Foundation v. Texas Equal Access to Justice* (*IOLTA I*), 873 F. Supp. 1 (W.D. Tex. 1995) aff'd in part, vacated in part, rev'd in part by 94 F.3d 996 (5th Cir. 1996) *r'hrg en banc* denied by 106 F.3d 640 (5th Cir. 1997) cert. granted in part by *Phillips v. Washington Legal Foundation (Phillips)*, 521 U.S. 1117 (1997) aff'd by 524 U.S. 156 (1998) appeal after remand by 86 F. Supp. 2d 624 (W.D. Tex. 2000) (*IOLTA II*) rev'd and remanded by 270 F.3d 180 (2001) (Wiener, J. dissenting).

of three questions raised by the case. That majority held that interest on funds deposited into lawyers' trust accounts is "property" of the client, but the same majority expressly left unanswered the other two questions:

> We express *no view* as to whether these funds have been "taken" by the State; nor do we express an opinion as to the amount of "just compensation," *if any*, due respondents. We leave these issues to be addressed on remand.[3]

The Court neither stated nor implied that prospective (injunctive) relief is even a possibility. Pursuant to the Supreme Court's directive and the crucial, far-reaching impact of the answers to these constitutional questions, this case and its implications at the circuit level of the fifty sovereign states should *not* have been left to the determination of but two (or even three if the panel had been unanimous) of our fifteen active judges.

Our panel majority's opinion and the Ninth Circuit's en banc opinion validate Justice Souter's worst concerns and predictions in *Phillips*.[20] In the eyes of the dissenting justices, the majority's recognition of the plaintiff's "abstract property right to interest 'actually earned'"[5] on his principal – severed from the inextricable questions whether a taking occurred and, if so, whether compensation is due – skewed the Fifth Amendment analysis.[6] Indeed, just as Justice

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[3] *Phillips*, 524 U.S. at 172 (Rehnquist, C.J.) (emphasis added).

[20] *Phillips*, 524 U.S. at 175-76, 178 (Souter, J., joined by Stevens, Ginsburg, and Breyer JJ., dissenting).

[5] *Id.* at 178.

[6] *Id.* ("One may wonder here not only whether the theoretical property analysis may skew the resolution of the taking and compensation issues that will follow, but also how far today's holding may unsettle accepted governmental practice elsewhere.")

Souter predicted, our district court's determination that the plaintiffs could not prove any amount of monetary loss under any accounting or economic theory demonstrates that the Supreme Court's abstract pronouncement in *Phillips* identified a right that exists in theory but is moribund in reality: With zero compensable loss, the abstract property right recognized by the Court has "no practical consequences for purposes of the Fifth Amendment."[7]

## II. *IOLTA II*

### A. *Takings: Ad Hoc versus Per Se Analysis*

A divided panel of this court has now established the Takings jurisprudence for this circuit regarding whether to use ad hoc or per se analysis when the property purportedly "taken" is money – more specifically, the illusory right to future interest, if any – that is both fungible and valued in dollars on its face. Consequently, determination whether the workings of IOLTA effect a taking depends largely on the analytical methodology employed by the examining court. The Ninth Circuit noted that, in Takings Clause cases, one or the other of two analyses – ad hoc or per se – has been employed.[8] Explaining that the per se analysis generally has not been used except in the context of real property, the Ninth Circuit determined that the ad hoc takings analysis is the correct method to apply when the property at issue is the mere intangible personal property right to *potential* interest, such as that which might accrue in IOLTA accounts.[9] In then

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[7] *Id.* at 174.

[8] *Id.* at 854 (citing *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982) (use of per se analysis); *Penn Central Transportation Co. v. City of New York*, 438 U.S. 104 (1978) (use of ad hoc analysis)).

[9] *Id.* at 856-57:

> Although we note that the Fifth Circuit recently has decided in a two to one decision to adopt the per se method of analysis in (continued...)

conducting its ad hoc assessment, the Ninth Circuit inspected (1) the economic impact of the regulation on the claimant, (2) the extent to which the regulation interfered with investment-backed expectations, and (3) the character of the governmental action.[10] Based on the unassailable truism that, absent the IOLTA program, the plaintiffs could not have recognized *any* net interest on their principal and that their investment position was no worse-off with IOLTA in place than without it, the court's ad hoc calculus revealed that no "taking" under the Fifth Amendment had occurred.[11]

Our analysis should have been guided by an understanding of the exact nature of the "property" at issue, not merely that, according to the Supreme Court, it is property. Here, we deal with neither tangible or intangible real property, nor even tangible personal property, such as a painting taken by a city for display in the Hotel de Ville. Rather, the "property" here at issue is the ephemeral net interest, if any, on a client's funds deposited into an IOLTA account, which can only produce net interest when combined with funds of other clients: Separately, the deposited funds are too few or are held too briefly to produce net interest for the individual client who owns the principal on deposit.

The only answer provided by the Supreme Court in *Phillips* is that this potential interest to be earned on funds in

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(footnote continued)

> similar (but not identical) circumstances, *given the monetary nature of the property in question, the public nature of the IOLTA program, and the highly-regulated nature of the banking industry, we believe the better approach is [the ad hoc analysis] of Penn Central.* (emphasis added) (citations omitted).

[10] *Id.* at 857

[11] In my panel dissent I assumed *arguendo* that a taking had occurred so as to reach the position that, even if there is a taking, it is unconstitutional *only* if done without just compensation.

an IOLTA account is property. Post *Phillips*, the first question we must answer – whether to apply ad hoc or per se analysis, or some yet unarticulated method to be used in situations when money is the purportedly taken property – is a novel and open one for our circuit, not to mention the entire federal system, save only the Ninth Circuit. Our panel majority's opinion assumes that the appropriation of IOLTA funds is a physical intrusion of property requiring application of the per se test articulated in *Loretto v. Teleprompter Manhattan CATV Corp.*[12] Like many of the cases employing per se analysis, however, *Loretto* involved only real property, making its application to the instant case a very questionable proposition. Whether appropriation of interest on an IOLTA account should be analyzed identically to physical invasions of real or tangible personal property is particularly important in light of the Supreme Court's recent directive:

> This longstanding distinction between acquisitions of property for public use, on the one had, and regulations prohibiting private uses, on the other, makes it inappropriate to treat cases involving physical takings as a controlling precedents for the evaluation of a claim that there has been a "regulatory taking," and vice versa.[13]

The key inquiry thus becomes whether appropriation of IOLTA funds is akin to the physical intrusion discussed in other per se cases. Scrutiny of (1) the original "fairness and justice" purposes of the Fifth Amendment, (2) the rationale

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[12] 458 U.S. 419 (1982) (holding that a takings had occurred by the fact of the physical intrusion of a cable company's cable on the roof of a privately owned building).

[13] *Tahoe-Sierra Preservation Council, Inc. v. Tahoe Regional Planning Agency*, 535 U.S. __, __, 122 S.Ct. 1465, 1479 (2002) (citation omitted).

underlying the per se doctrine, (3) the methodology employed by takings cases involving money or monetary liability, in addition to (4) a thorough evaluation of the cases purportedly supporting application of the per se doctrine, makes clear that this doctrine, as it is used in cases dealing with real or tangible personal property, is ill-suited to analyze the instant case, which involves intangible personal property in the form of potential interest on principal.

**B. *Fairness and Justice***

The original purpose of the Fifth Amendment reflects an understanding that situations like the one presented by IOLTA do not fall neatly into any particular takings analysis. One of the Supreme Court's venerable Takings Clause cases, *United States v. Armstrong*, teaches that "The Fifth Amendment's guarantee that private property shall not be taken for public use without just compensation was designed to bar Government from forcing some people alone to bear public burdens, which, in all fairness and justice, should be borne by the public as a whole."[14] Here, no one, including the plaintiffs, is being asked to "bear" a public burden in any sense that impinges on the notions of fairness and justice. In fact, the evidence presented in the district court clarifies that absolutely no hardships are borne by the plaintiffs as a result of IOLTA – their position, vis-à-vis Takings Clause law, is exactly the same with or without IOLTA, relegating their dubious complaints solely to the realm of the First Amendment.

It is indeed a novel extension of Fifth Amendment jurisprudence to allow these plaintiffs to prevail without any showing of loss or hardship. In fact, in this case, it is the prescribing of injunctive relief that assaults the notions of

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[14] 364 U.S. 40, 49 (1960).

fairness and justice underlying the Amendment. It is the plaintiffs – accused by some of playing the dog in the manger[15] – who, begrudging others what they cannot themselves enjoy, seek to dismantle a program that promotes the public good without placing undue burdens on any one person or group.

### C. *Incongruous Rationale Underlying the Per Se Doctrine*

*Loretto* explains the rationale for employing the per se analysis in physical invasion cases: "Property rights in a physical thing have been described as the rights 'to possess, use and dispose of it.' To the extent that the government permanently occupies physical property, it effectively destroys *each* of these rights."[16] This rationale, although convincing in the context of real and tangible personal property, is inapt when the property at issue is the speculative interest on the plaintiffs' pooled funds in an IOLTA account: unpooled, such principal could not generate net interest. Without Congress's enactment of 12 U.S.C. § 1832, which permitted the creation of NOW accounts, a client's principal would have absolutely no economic value to the client beyond the value of the principal itself.[17] Therefore, unlike real or tangible personal property, the plaintiffs' property

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[15] *See* Donald L. Beschle, *The Supreme Court's IOLTA Decision: Of Dogs, Mangers, and the Ghost of Mrs. Frothingham*, 30 Seton Hall L. Rev. 846, 867 (2000); *see also*, Aesop, *Aesop's Fables 1* (Grosset & Dunlap, eds. 1947) (describing a dog that cannot derive beneficial use of straw, but inexplicably, perhaps for some perverse satisfaction, denies an ox that eats the straw access to it; the author includes the story's moral: "Ah, people often grudge others what they cannot enjoy themselves.").

[16] *Loretto*, 458 U.S. at 435 (emphasis in original) (citation omitted).

[17] The interest that accrued on those accounts would be forfeited to the banks which held the accounts. *See IOLTA II*, 270 F.3d 180, 182-83 (5th Cir. 2001).

right to receive interest on their principal, with or without IOLTA, is a kind of property that its owners cannot actually "use" or "dispose" of, even if it is, hypertechnically, their property.

The Supreme Court, in deciding that the interest on IOLTA accounts is property, noted that valuable rights other than economic rights appertain to property. Specifically, the Court's majority opinion states that "[w]hile the interest at issue here may have no economically realizable value to its owner, possession, control, and disposition are nonetheless valuable rights that inhere in property."[18] Even though, as an abstract universal proposition, this is undoubtedly true, the Court did not inform us just what those other "valuable rights" would be in the context of the specific property at issue. I find perplexing the Court's statement that property may still have value, other than its pure monetary value, given the context of the kind of property here at issue – money. With the utmost respect (and at the risk of revealing my own intellectual shortcomings), I read the Court's opinion in *Phillips* as begging the question of what other "valuable rights" inhere with the ownership of money, which, axiomatically, can only be defined by its face value.

Second, none dispute that, even without IOLTA, the plaintiffs cannot physically "possess" this chimeric interest or even "control" where these funds end up. The plaintiffs' mythical "choice" is between allowing banks to gobble the interest, using each client's principal as an interest-free loan, on the one hand, or allowing the lawyers of Texas, under the supervision of the Texas Supreme Court, to fulfill the legal profession's ethical duty to the needy by diverting the interest to legal aid societies, on the other. Put simply, the "valuable rights" other than economic value that appertain to

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[18] *Phillips*, 524 U.S. at 170.

real or tangible personal property simply do not exist when the property at issue is potential interest on a principal amount that alone is too small or held too fleetingly to generate net interest for its owner.

When carefully assayed, the property at issue in IOLTA constitutes a unique variety that does not easily conform to the traditional rights attendant on real or tangible personal property. Understanding this, Justice Souter stated in dissent that "it is enough to note the possible significance of the facts that there is no physical occupation or seizure of tangible property, that there is no apparent economic impact . . . ."[19] This observation demonstrates that, even though the Supreme Court decided that the interest on IOLTA accounts is property, the Court has not yet identified the type of taking, if a taking at all, that is effected by appropriation of IOLTA interest.

The difficulty in evaluating the type of analysis that is appropriate for IOLTA funds is especially important in light of the Supreme Court's explanation that "physical appropriations are relatively rare, easily identified, and usually represent a greater affront to individual property rights."[20] The Ninth Circuit's en banc analysis and my dissent in this circuit's *IOLTA II* case, not to mention the 5-4 divided Supreme Court, confirms that we are not presented with a situation that is susceptible of easy legal categorization, a fact that militates against the panel majority's per se analysis. In this case, and possibly all others involving a monetizable interest, the per se doctrine – adopted from the Supreme Court's rulings in real and

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[19] *Id.* at 176 (Souter, J. dissenting).

[20] *Tahoe-Sierra*, 535 U.S. at ___, ___122 S.Ct. at 1479 (discussing the contrast between regulatory takings of real property and physical intrusions on real property).

tangible personal property cases – is a blunderbuss approach to an issue that requires target-rifle accuracy.

### D. *Balancing Approach Employed in Takings Cases Involving Money*

Unfortunately, the few cases that address the Takings Clause in the context of money are not wholly on point. They do, however, confirm that when the property at issue is money, a distinct analysis – separate from per se or ad hoc, or any other method used for real and tangible personal property – is required. Both *Webb's Fabulous Pharmacies, Inc. v. Beckwith*[21] and *United States v. Sperry Corp.*[22] are "fee for services" cases which were decided by assessing the relationship between the amount of money withheld by the governmental entity and the service provided by the government for which the money was withheld (court fees in *Webb's*, claims tribunal in *Sperry*). Although the Court held that a takings occurred in *Webb's* when the government appropriated an interpleader accounts' interest, the facts of Webb are inapposite to the instant case despite their superficial similarity. *Webb's* would be analogous to the case before us *only if* IOLTA programs indiscriminately appropriated the interest from a client's principal, whether or not on its own that principal would have earned net interest the receipt of which the client had a legitimate expectation. The defining terms of the IOLTA program, however,

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[21] 449 U.S. 155 (1980) (holding that the court clerk's appropriation of the interest on funds held by the court in an interpleader action was an unconstitutional taking because the funds were held for the benefit of creditors and the amount withheld was not reasonably related to services rendered by the court).

[22] 493 U.S. 52 (1989) (holding that withholding of a small percentage of an award from Iran-United States Claims Tribunal was not an unconstitutional taking because the amount was not clearly excessive as a user fee).

preclude this result by barring the deposit of that category of client funds into IOLTA accounts.[23]

More importantly, the focus in *Webb's* and *Sperry* is on the reasonableness of the relationship between the appropriated amount and the reasons for the appropriation, suggesting that, in the context of money, the Supreme Court *does not apply* the same per se analysis it uses in the context of real and tangible personal property. Without question, in both cases the governmental entity forthrightly took control of the funds, but in neither case was the taking by itself determinative of the outcome. Significantly, one of the dispositive factors in *Webb's* was that "Webb's creditors...had more than a unilateral expectation" in the accruing interest and that "it was property held only for the ultimate benefit of Webb's creditors."[24] In contrast, the plaintiffs here cannot possibly have any financial expectation (unilateral or otherwise) in the interest from the IOLTA account – their funds could never gain net interest for them, even without IOLTA.[25]

In all likelihood, these specific concerns, which arise when the property at issue is money, are what prompted the Court to remark in *Sperry* that "[i]t is artificial to view deductions of a percentage of a monetary award as physical appropriations of property. Unlike real or personal property,

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[23] TEAJF Rule 6 (Client funds may be deposited in an IOLTA account only if those funds "could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the account . . . .")

[24] *Webb's*, 449 U.S. at 451.

[25] *See supra* note 23.

money is fungible."[26] In both *Webb's* and *Sperry* the Court engaged in an implicit weighting of factors, similar to that undertaken in a case expressly employing ad hoc analysis, to determine the reasonableness of the appropriations involved.

This theme as articulated in *Sperry* – that money is a unique type of property which is inadequately covered by conventional real or personal property analysis – is reflected in two subsequent appellate court cases. In *Nixon v. United States*, the D.C. Circuit held that personal property is subject to *Loretto's* per se doctrine. In doing so, however, the court expressly described *Sperry* as clarifying that, although real and personal property are subject to the doctrine, money does not receive per se analysis.[27] More recently, in *Branch v. United States*, holding that the Fifth Amendment was not violated by the federal government's seizure of one bank's assets to offset losses of another bank owned by the same bank holding company, the Federal Circuit stated that "[b]ecause of 'the State's traditionally high degree of control of commercial dealing,' the principles of takings law that apply to real property do not apply in the same manner to statutes imposing monetary liability."[28] Seeming to foreshadow the unique nature of IOLTA, the *Branch* court, using *Sperry* as its paradigmatic example, continued: "Nor

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[26] 493 U.S. at 62, n. 9. Contrary to Judge Kozinski's argument in his dissent from the Ninth Circuit's en banc opinion in *WLF v. LFW*, fungibility is relevant and important. It not only affects the choice of Supreme Court precedent to be applied, but, as discussed further below, obviates and renders inapt injunctive remedies.

[27] 978 F.2d 1269, 1285 (D.C. Cir. 1992) (the court's parenthetical explanation of *Sperry* following its citation of that case reads: "distinguishing between money, which is not subject to the per se doctrine because it is fungible, and 'real or personal property'").

[28] 69 F.3d 1571, 1576 (Fed. Cir. 1996) (quoting *Lucas v. South Carolina Coastal Council*, 505 U.S. 1003 (1992)).

are other, less conventional assessments viewed as per se takings, requiring compensation without inquiry into their reasonableness."[29]

The Texas IOLTA program is nothing if not a "less conventional" method of regulating financial dealings with commercial institutions so as to fulfill the legal profession's ethical obligation to the underprivileged members of society. Thus, the panel majority's application of the per se doctrine, in the form developed for real and personal property *other than money*, is a highly questionable proposition that suffers from two palpable analytical flaws: (1) It is not grounded in definitive or wholly applicable Supreme Court precedent; and (2) it fails to address the special treatment accorded by the Supreme Court and other appellate courts to situations in which the property purportedly taken is money.

### E. *Inadequate Case Law Support for Application of Per Se Analysis*

A closer study of the four cases relied on here by the panel majority to reach its conclusion regarding the per se doctrine further illustrates the weakness of the panel's argument.[30] According to the panel majority, *Phillips*, and *Webb's* and *Loretto* (the two cases on which *Phillips* relied), "compel applying the per se analysis."[31] I must disagree: The analysis in *Phillips* mandates no such method; the Court specifically answered only the question whether the interest on IOLTA accounts was property, expressly pretermitting any discussion of takings and just compensation. The Court's majority opinion cites *Webb's* only for the

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[29] *Id.*

[30] *See Phillips*, 524 U.S. 156; *Lucas*, 505 U.S. 1003; *Webb's*, 449 U.S. 155; *Loretto*, 458 U.S. 419.

[31] 270 F.3d at 186.

proposition that interest follows principal, and cites *Loretto* only for the proposition that an item can be property without having a positive economic or market value. Thus, the panel majority's reading unduly strains the plain language of *Phillips*. The simple fact of the Court's reliance on *Webb's* and *Loretto* for the "property" analysis does not dictate application of those cases to the takings question.

Furthermore, as discussed above, those case are factually and legally distinguishable from the instant case, making any rote application of their reasonings or holdings simplistic and incongruous. *Webb's* was a user-fee case that did not address either per se or ad hoc approaches, instead basing its holding on (1) the legitimate expectation of accrued interest by creditors, and (2) the arbitrary relationship between the amount taken and any service rendered by the government.[32] *Loretto* implicated an actual, physical occupation of real property by a cable company's lines. As the Court was dealing with a brick-and-mortar item, the presence of the cable lines actually did interfere with other "valuable rights" such as the right to control, dispose of, and otherwise profit from the physical space occupied by the cables. It is these prototypical physical invasion cases (and parallel tangible personal property cases) for which the Supreme Court created per se analysis in the first place, and it is only these to which the analysis has been applied. No case cited by the panel majority or written by

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[32] As already stated, the Court's focus on these factors in *Webb's* implicitly endorses a non-categorical approach to takings analyses that involve money. The panel majority's focus on the "factual similarity" of Webb's is misleading because the cases would be factually analogous *only if* clients whose principals could, on their own, earn net interest were pooled in an IOLTA account despite those clients' legitimate expectations of possessing the interest on their principals.

the Supreme Court has rotely applied the per se doctrine to the putative taking of money or a monetizable interest.

With similar fallacy, the panel majority reads *Loretto* to stand for the proposition that physical occupation of property constitutes a per se taking "*regardless* of the economic impact on the owner."[33] The holding of *Loretto*, however, is much narrower: The physical invasion of *real* property, no matter how *minimal*, is a per se taking. Specifically, the *Loretto* court stated that a permanent physical occupation is a per se taking even if the action "has only *minimal* economic impact on the owner [of the real estate]."[34] Thus, *Loretto* did not answer the more difficult question of how to assess a purported taking with *no* economic impact on property that is only valued monetarily – money. The panel majority's invoking of *Loretto* still leaves three issues unsatisfactorily unresolved: (1) whether appropriation of potential net interest from pooled principals, which principals by themselves could not produce net interest, is a physical invasion or occupation; (2) whether the takings analysis for real or tangible personal property is applicable to the purported taking of potential interest; and (3) what is the proper treatment of monetary appropriations that have no economic impact on the property owner whatsoever.

Finally, *Lucas*, another case cited by the panel majority in an effort to support its application of per se takings analysis, provides only paper-thin support, if any support at all, for the panel majority's position. In *Lucas*, the Court dealt with a *regulatory* taking of real property. Even though it was a regulatory taking and not a physical invasion, the Court abandoned the ad hoc test of *Penn Central* and

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[33] 270 F.3d at 187 (emphasis added).

[34] 458 U.S. at 435.

declared the regulation a taking because it had caused the property owner to "sacrifice *all economically beneficial*" uses of his property.[35] If the panel majority truly wants to apply *Lucas* to the instant case, then the relevant inquiry must be whether IOLTA strips the plaintiffs of all *economically beneficial* use of their property (i.e., their interest). Simply and accurately, the answer is no. Even absent IOLTA, the plaintiffs cannot use the interest on their principals because their funds will not gain net interest; therefore, by definition, vis-à-vis the plaintiffs, there is no such thing as an economically beneficial use that the government could have taken. The plaintiffs' counter argument – that, even though no economic benefit is lost through the program, IOLTA robs them of the subjective benefit of letting their speculative interest lie fallow – is not a takings claim; at most, it is a dubious First Amendment claim.

The panel majority's reliance on *Lucas* is rendered even more tenuous by the Supreme Court's statement in that case regarding the treatment of commercial dealings. Discussing the regulatory taking of real property, the Court in *Lucas* declared

> It seems to us that the property owner necessarily expects the uses of his property to be restricted, from time to time, by various measures newly enacted by the State in legitimate exercise of its police power; . . . And in the case of personal property, by reason of the State's traditionally high degree of control over commercial dealing, he ought to be aware of the possibility that new regulation might even render his property

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[35] 505 U.S. at 1019 (emphasis added).

> economically worthless (at least if the property's only economically productive use is sale or manufacture for sale). In the case of land, however, . . . ."[36]

This statement in *Lucas*, read in conjunction with the Federal Circuit's approach in *Branch*,[37] casts even greater doubt on the panel majority's decision to subject the potential interest here at issue to the doctrines used to evaluate takings of real property and personal property other than money. Far from "compelling" a per se approach, the panel majority's analysis belies the complexity of established Takings Clause precedent and avoids tackling the demanding questions presented by a taking of monetizable property as distinguished from real and tangible personal property.

### III. *The Amount of Just Compensation Due, If Any*

The second question left open by the Supreme Court's opinion in *Phillips* is what just compensation, if any, is due. Consistent with my dissent but contrary to the panel majority's view, the Ninth Circuit held that, even if there were a "taking" of property," it was not done without just compensation: Just compensation for zero is zero. Relying on Justice Holmes statement in *Boston Chamber of Commerce v. City of Boston* that "the question is What has the owner lost? not What has the taker gained[,]" the Ninth Circuit sought to determine what the plaintiffs would have gained in the absence of IOLTA.[38] Concluding that the most that the plaintiffs lost was the esoteric right to prevent their principal from earning interest (presumably only because

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[36] *Id.* at 1027-28.

[37] *See supra* notes 27-28 and accompanying text.

[38] 271 F.3d at 862 (quoting *Boston Chamber of Commerce v. City of Boston,* 217 U.S. 189, 195 (1910)).

they opposed the government's making use of that interest without their consent – or downright disapproval of the uses to which "their" interest would be put), that court found that the plaintiffs suffered neither economic loss nor the loss of a right with economic value.

The Supreme Court's opinion in *Phillips* neither decreed nor compelled an answer to the just compensation question; in fact, the *Phillips* majority specifically wrote that "whether client funds held in IOLTA accounts could generate net interest *is a matter of some dispute*."[39] Traditionally, the resolution of these factual disputes is the province of the district court. Here, following remand, presentation of testimony, and hearings regarding various accounting and economic theories, the district court determined, as a factual matter, that individual client funds could not generate net interest and therefore the plaintiffs' loss totaled zero dollars. The plaintiffs essentially conceded this point, and none contends that this finding is clearly erroneous. The district court's factual finding in this regard should erase the doubts expressed by the *Phillips* majority, as no dispute should currently exist: When no just compensation is due, the taking is not unconstitutional.

Keeping the finding of zero compensable loss firmly in mind, our panel should have followed the chronological analysis prescribed for all takings cases: First determine whether a takings occurred, and then determine the amount of just compensation, if any, that is due. Importantly, the Fifth Amendment has never been read to proscribe a taking *vel non*;[40] rather it is a constitutional guarantee that anything

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[39] 524 U.S. at 169 (emphasis added).

[40] *First English Evangelical Lutheran Church of Glendale v. Los Angeles* (*First English*), 482 U.S. 304, 314 (1987) ("As its language indicates, and as the court has frequently noted, [the Fifth Amendment] *does not* (continued...)

taken will be justly compensated for, if necessary.[41] Thus, the logic that flows from this established understanding of the Fifth Amendment is that a takings by itself, even one that is a per se taking, is not unconstitutional; only failing to compensate the dollar value of any resulting loss is unconstitutional. Incredulously, by invoking the ripeness doctrine, the panel majority turned this straightforward and controlling approach on its head, opting instead for a circular analysis that finds no support in logic or case law.

Assuming, *arguendo*, that a takings occurred (whether per se or otherwise), the proper analysis of IOLTA should have proceeded thusly: (1) The potential interest on an IOLTA account is property; (2) a taking occurred (my *arguendo* assumption); but (3) the plaintiffs demonstrated a monetary loss of zero as determined by the district court's extensive fact-finding; so (4) the amount of just compensation due to the plaintiffs is zero; (5) the taking (whether per se or otherwise) is not unconstitutional; ergo, no remedy is required. Instead of dealing with the just compensation determination in this direct manner, as it should have, the panel majority instead jumped from a finding of a per se taking to a *prohibition* of the taking through injunctive relief – the exact result proscribed by the Supreme Court in *First English*.[42]

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(footnote continued)

*prohibit the taking of private property*, but instead places a condition on the exercise of that power.") (emphasis added).

[41] *Id.* ("This basic understanding of the Amendment makes clear that it is designed not to limit the governmental interference with property rights *per se*, but rather to secure *compensation* in the event of otherwise proper interference amounting to a taking.") (emphasis in original).

[42] *Id.*



When reduced to its essentials, the panel's novel methodology appears to proceed in this order: (1) the potential interest on the IOLTA accounts is property; (2) a per se takings occurred under *Loretto*; (3) having determined that a per se taking of property occurred, the district court's finding of zero loss is irrelevant; (4) because a takings has occurred there must be some available remedy (even though none is mentioned in the Constitution) regardless of the district court's finding; so (5) in the absence of provable loss, the appropriate remedy is injunctive relief, a prophylactic which prohibits the taking rather than simply placing a condition on it. This logic is a perversion of all established Fifth Amendment jurisprudence and finds absolutely no support in case law.

Under the instant facts, the rule should be that when the allegations specify that a monetary interest was taken, what follows from the finding of zero loss is *not* that declaratory and injunctive must be awarded, but rather that the taking is not unconstitutional. The panel majority has conflated (1) its determination that the appropriation of IOLTA interest is a per se taking with (2) the determination that it is also per se unconstitutional. This conflation puts the proverbial cart before the horse: Finding no provable economic loss (for the alleged taking of money), but somehow convinced of the impropriety of the transaction and thus the need to find a remedy, the panel majority retroactively searches for the only other possible remedy available – injunction.

But again, this novel creation produces a flawed methodology. The plaintiffs in this case do not receive monetary compensation because they have lost nothing of economic value, putting the lie to their claim that the government has unconstitutionally taken their property

(specifically, their speculative interest from their contribution to the pooled principal in the IOLTA account).[43] The very fact of their inability to prove a compensable monetary loss should end the case, not trigger a search for alternative equitable remedies. The absence of value means, quite straightforwardly, that the appropriation of the plaintiffs' property in this case is not proscribed by the Fifth Amendment.

Finally, even if the panel majority's per se analysis were to be accepted, injunctive relief, although the only potential remediation available to a plaintiff with no provable loss, is wholly inappropriate. Rather than fabricating jurisprudence that seeks to match some remedy with a perceived constitutional violation, the direct (and correct) approach is to provide the expressly prescribed constitutional remedy. In this case, because money is the only property alleged to have been taken – and because money is fungible – the only remedy is the payment of just compensation in money. This leads to the absurdity of taking a dollar and, in return, compensating the former owner with a dollar. Unlike other personal property, which may have no market value but possibly has enough subjective personal value, e.g., sentimental or historical, to justify an injunction, money is defined only by its facial economic value. Most importantly, an injunction in this case contravenes the fundamental dictates of Fifth Amendment jurisprudence by prohibiting the taking of property even though the government stands willing to pay just compensation.

Furthermore, given the nature of the property at issue, agreement with the Ninth Circuit's *en banc* position or my

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[43] *See United States v. Causby*, 328 U.S. 256, 261 (1946) ("It is the owner's loss, not the taker's gain, which is the measure of the value of the property taken.").



dissent does *not* equate to subscribing to a blanket rule that the taking of property of no fair-market value results in a rule that no unconstitutional taking has occurred each and every time. I recognize, for example, that if, as part of its permanent retrospective on its founders, a town wants to take Aunt Bertha's amateurish self-portrait (with zero net fair market value), or if, for its historical display, a city wishes to take the remains of a chimney (with zero net market value) from a burned-down house on my old home place, such governmental actions may well constitute "takings" of "property" that might properly be addressed with injunctive relief. But when the taken property is dollars (or, more accurately, the abstract right to potential dollars of net interest earned when one client's principal is pooled with the principal of other clients of the law firm), declaratory or injunctive relief is, at best, a highly questionable proposition. Loss of a "monetizable" interest is a stereotypical example of a situation in which there need be no relief, injunctive or otherwise. When – more accurately, if – the plaintiff/client can prove an actual dollar loss, he can be compensated fully for that loss and be made whole, without resorting to declaratory or injunctive relief; if he cannot prove deprivation of actual monetary value, his redress against the taker must be at the ballot box, not in court.

As I noted in my panel dissent, "our" district court found that under any applicable accounting method or economic analysis – either in-firm pooling, sub-accounting, or net-benefit theory – the plaintiff/client (Summers) suffered no loss. Put simply, Summers is in exactly the same financial position with the IOLTA program in place as he would be in its absence. As he complains of an outright financial taking (and not the taking of either real or tangible, personal property), our most straightforward approach would be – and should be – to determine the exact dollar amount purportedly confiscated from Summers.

As a factual matter, the district court found (as did the Ninth Circuit regarding similarly situated plaintiffs) that the plaintiff's compensable loss – past, present, and future – summed to *zero* dollars. Thus, although Summers complains of the confiscation of his property right to interest, he cannot under any accounting theory or economic analysis establish a dollar – or cents! – figure that is owed to him by the governmental taker. He presents a perfect illustration of Justice Holmes's point: Although the state (actually, various legal services organizations) gained money, Summers was deprived of none.

## IV. *Conclusion*

Vested with the constitutional authority to regulate the legal profession – the state's recognition of classic republican separation of powers – the Texas Supreme Court created the Texas IOLTA program to address, *inter alia*, lawyers' ethical responsibility to provide legal services to the poor. Even if – unlike real or tangible personal property – the interest earned (or to be earned) on lawyers' trust accounts that is used to fund those services is, hypertechnically, the "property" of the owners of the principal, those owners must show monetary loss before they can state a Fifth Amendment claim to be compensated by the state. But, they cannot show such a loss, so they cannot state such a claim: Absent a showing of loss, any allegedly uncompensated "taking" by the state is constitutionally permitted. Unlike the tangible property illustrations, a taking of an intangible financial right with *no* market value – and thus not subject to being taken unconstitutionally – cannot lead alternatively to an enjoined, prior-restraint proscription of the taking.

As I disagree with the reasoning and result of the panel majority opinion, I respectfully dissent from denial to rehear this case en banc *and*, as a result of that denial, from failing to reinstate the ruling of the district court.

UNITED STATES COURT OF APPEALS
FOR THE FIFTH CIRCUIT

No. 95-50160

WASHINGTON LEGAL FOUNDATION; William R. Summers; Michael J. Mazzone,

Plaintiffs-Appellants,

v.

TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; W. Frank Newton, Chairman, Texas Equal Access to Justice Foundation; Thomas R. Phillips, Chief Justice; Raul Gonzalez, Justice; Jack Hightower, Justice; Nathan L. Hecht, Justice; Lloyd A. Doggett, Justice; Bob Gammage, Justice; Craig T. Enoch, Justice; John Cornyn, Justice; Rose Spector, Justice; Supreme Court DFTS,

Defendants-Appellees.

February 14, 1997

Appeal from the United States District Court for the Western District of Texas; James R. Nowlin, Judge.

ON PETITIONS FOR REHEARING AND
SUGGESTIONS FOR REHEARING EN BANC

September 12, 1996

Before *WISDOM*, *GARWOOD* and *JONES*, Circuit Judges.

PER CURIAM:

The Petitions for Rehearing are DENIED and the court having been polled at the request of one of the members of the court and a majority of the judges who are in regular active service not having voted in favor, (FRAP and Local Rule 35) the Suggestions for Rehearing En Banc are also DENIED.

POLITZ, Chief Judge, and KING, WIENER, BENAVIDES, STEWART and PARKER, Circuit Judges, dissent from the refusal of the court to grant rehearing en banc.

DENNIS, Circuit Judge, did not participate.

BENAVIDES, Circuit Judge, joined by POLITZ, Chief Judge, and STEWART and PARKER, Circuit Judges, dissenting from failure to grant rehearing en banc:

In the subject case, a panel of this court held that "clients . . . have a cognizable property interest in the interest proceeds that are earned on their deposit in IOLTA accounts." 94 F.3d 996, 1005 (5th Cir.1996). In reaching this conclusion, the panel relied upon the traditional rule applied in Texas that "interest follows principal," which recognizes that interest earned on a deposit belongs to the owner of the principal. *Id.* at 1000. The panel also relied upon the Supreme Court's opinion in *Webb's Fabulous Pharmacies, Inc. v. Beckwith,* which in turn relied upon the same state law rule to hold that "earnings of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property." *Id.* at 1002 (quoting 449 U.S. 155, 164, 101 S.Ct. 446, 452-53, 66 L.Ed.2d 358 (1980)).

This decision is an important one because it contradicts every other court in the country that has

addressed this issue, including two of our sister circuits and a large number of state appellate courts.[21] Moreover, while purporting to resolve only a threshold issue in this case, the opinion is bound to create difficulties and confusion for the district court on remand. Finally, this case poses an unwarranted threat to a primary source of funding for public interest legal organizations in this circuit at a time when these organizations are already struggling for their lives financially. For the foregoing reasons, I believe that this case is worthy of our en banc consideration and respectfully dissent from the contrary conclusion of my colleagues.

I.

Texas is one of fifty states that operates an Interest on Lawyers Trust Account Program ("IOLTA"). The IOLTA concept is possible because there are situations in which the costs of maintaining funds held by lawyers for their clients exceed the interest that a client can earn from a financial institution. When the amount of a client's funds to be held is nominal or when a client's funds will be held for a brief period of time, the deposit of a client's funds acts as an interest-free loan to the bank. IOLTA is an attempt to

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[21] *See Washington Legal Fdn. v. Mass. Bar Fdn.*, 993 F.2d 962 (1st Cir.1993); *Cone v. State Bar of Fla.*, 819 F.2d 1002 (11th Cir.), *cert. denied*, 484 U.S. 917, 108 S.Ct. 268, 98 L.Ed.2d 225 (1987); *Carroll v. State Bar of Cal.*, 166 Cal.App.3d 1193, 213 Cal.Rptr. 305 (Cal.Ct.App.1984), *cert. denied*, 474 U.S. 848, 106 S.Ct. 142, 88 L.Ed.2d 118 (1985); *Petition by Mass. Bar Ass'n*, 395 Mass. 1, 478 N.E.2d 715 (1985); *In re Interest on Lawyers' Trust Accounts*, 279 Ark. 84, 648 S.W.2d 480 (1983); *In re Adoption of Amendments to C.P.R.D.R.* 9-102 IOLTA, 102 Wash.2d 1101 (Wash.1984); *In re Lawyers' Trust Accounts*, 672 P.2d 406 (Utah 1983); *In re New Hampshire Bar Ass'n*, 122 N.H. 971, 453 A.2d 1258 (1982); *In re Minnesota State Bar Ass'n*, 332 N.W.2d 151 (Minn.1982); *In re Interest on Trust Accounts*, 402 So.2d 389 (Fla.1981).

transfer this benefit from banks to legal providers for the indigent. The Texas IOLTA program has been a resounding success, raising approximately $10 million per year for legal services organizations in the state.

The plaintiffs brought this action because of their objections to the activities of the recipients of IOLTA funds.[22] *Washington Legal Fdn.*, 94 F.3d at 999. The plaintiffs contend that the IOLTA program constitutes an unconstitutional taking of property, in violation of the Fifth Amendment to the United States Constitution, and that the program violates the First Amendment because it forces them to support speech they find offensive. The plaintiffs seek an injunction against further operation of the Texas IOLTA program and compensation for any interest earned on their deposits into IOLTA accounts.

The district court concluded that the plaintiffs' constitutional challenges failed at the threshold because the plaintiffs could not establish a property interest in the earnings from funds deposited in IOLTA accounts. The district court, therefore, granted summary judgment in favor of the defendants. On appeal, a panel of this court reversed the decision of the district court and remanded the case for further proceedings.

II.

"The pertinent words of the Fifth Amendment of the Constitution of the United States are the familiar ones: 'nor

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[22] IOLTA rules provide that "[t]he Foundation shall make grants to organizations . . . hav[ing] as a primary purpose the delivery of legal services to low income persons . . . ." TEXAS RULES OF COURT-STATE, Rules Governing the Operation of the Texas Equal Access to Justice Foundation ("IOLTA Rule"), Rule 10 (West 1996). Eligible recipient organizations "shall use such funds to provide legal services to individual indigent persons." IOLTA Rule 11.

shall private property be taken for public use, without just compensation.'" *Webb's Fabulous Pharmacies,* 449 U.S. at 160, 101 S.Ct. at 450. In order to prevail on a takings clause claim, a plaintiff must establish an interest in private property. "Property interests . . . are not created by the Constitution. Rather, they are created and their dimensions are defined by existing rules or understandings that stem from an independent source such as state law." *Board of Regents v. Roth,* 408 U.S. 564, 577, 92 S.Ct. 2701, 2709, 33 L.Ed.2d 548 (1972). "But a mere unilateral expectation or an abstract need is not a property interest entitled to protection." *Webb's Fabulous Pharmacies,* 449 U.S. at 161, 101 S.Ct. at 451.

At the outset, it is important to draw a distinction never addressed by the panel between "accrued interest" and "interest proceeds." The panel correctly noted that accrued interest is always created by funds deposited in a bank. *See Washington Legal Fdn.,* 94 F.3d at 1003. The IOLTA concept is simply an attempt to transfer this accrued interest from banks to legal aid organizations. Interest proceeds, however, are the amount of accrued interest that remains after deducting the costs of administering a deposited fund. It is undisputed that a client's funds may be deposited in an IOLTA account only if they are incapable of producing interest proceeds because of the nominal amount or the short duration of the deposit.[23]

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[23] IOLTA Rule 6 provides, in part:

> The funds of a particular client are nominal in amount or held for a short period of time, and thus eligible for use in the Program, if such funds, considered without regard to funds of other clients which may be held by the attorney, . . . could not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset the cost of establishing and maintaining the

(continued...)

A careful reading of *Webb's* makes clear that the existence of interest proceeds to which the depositors were entitled was a prerequisite to the Court's decision. In reaching its conclusion that creditors had a cognizable property right to the interest from an interpleader fund deposited with the court clerk for their benefit, the Court held that "[t]he *earnings* of a fund are incidents of ownership of the fund itself and are property just as the fund itself is property." *Webb's Fabulous Pharmacies,* 449 U.S. at 164, 101 S.Ct. at 452 (emphasis added). A clear implication of this holding is that if a fund generates no earnings to which its owner is entitled, there is no cognizable property interest.

Moreover, when the Court discussed whether the creditors had a property interest in the principal of the interpleader fund, the Court recognized that "[i]t is true, of course, that none of the creditor claimants had any right to the deposited fund until their claims were recognized and distribution was ordered." *Id.* at 161, 101 S.Ct. at 451 (citation omitted). In concluding that the creditors did in fact have a property interest, the Court was careful to note that "[e]ventually, and inevitably, that fund, less proper charges authorized by the court, would be distributed among the creditors as their claims were recognized by the court." *Id.*

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(footnote continued)

> account, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain interest on such funds for the client.
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> It is worth noting that whether attorneys correctly apply the requirements of Rule 6 is irrelevant to the constitutional issue resolved by the panel's opinion. If attorneys violate IOLTA's rules by depositing ineligible funds, it seems that any action a client might have would be against her attorney. To the extent the state may be implicated, this is certainly not because IOLTA's rules result in the taking of a client's property, but rather because IOLTA's rules were not followed.

This language makes clear that the Court will not recognize a constitutionally cognizable interest in the principal of a deposited fund unless and until it is clear that the fund will be distributed as proceeds to its beneficiary. Therefore, when the Court later concluded that earnings from such a fund are property "just as the fund itself is property," *id.* at 164, 101 S.Ct. at 452, the Court strongly suggested that interest proceeds are a necessary prerequisite to a constitutionally cognizable property interest in the earnings from a deposited fund.

Finally, the Court was careful to limit its holding to cases in which a separate statute authorizes the state to subtract its administrative costs. *See id.* at 164-65, 101 S.Ct. at 452-53. In those cases it is clear that interest proceeds exist because the costs of administering the fund have already been subtracted from the accrued interest generated by the fund. Therefore, it is equally clear that the fund's owner has been deprived of a property interest. In cases where "double tolling" of this sort does not occur, it cannot be so easily determined whether the fund's owner has been deprived of interest proceeds to which she is entitled. It is clear to me that the Court limited its holding because a bright-line rule establishing a property interest in this latter situation would be inappropriate.

Similarly, it follows that the state law rule that "interest follows principal" controls only when interest is earned on the principal or, in other words, when interest proceeds are available.[24] Consider the fate of the plaintiffs' accrued interest in the absence of IOLTA. Because the costs

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[24] The *Webb's* Court's limitation of its holding would have been unnecessary if the "interest follows principal" rule results in the creation of a property interest irrespective of the costs associated with administering accrued interest.

of administering the deposited funds would exceed any interest earned by a client, the bank would keep the accrued interest. Are the banks violating the traditional state law rule? Are the banks somehow converting or stealing the clients' property? The answer of course is no-because the clients had no interest in property to take.

III.

The panel attempted to avoid this reality by claiming that a bank assigns interest to a depositor in a two-part process. *See Washington Legal Fdn.*, 94 F.3d at 1003. According to the panel, a bank attributes interest to an account prior to deducting any of its fees. *Id.* From this, the court concluded that "a property interest attaches the moment that the interest accrues. . . ." *Id.*

Even if the panel presents an accurate picture of banking practices, however, those practices are beside the point. For purposes of a takings clause challenge, a constitutionally cognizable interest in property does not exist in "earnings" from a deposited fund unless and until those earnings can be distributed as proceeds to the fund's beneficiary. Because IOLTA-eligible funds would never produce interest proceeds, earnings from such funds cannot be distributed to the funds' owners. For this reason, the panel's conclusion that a property interest was created after the first step in the bank's process of assigning interest is simply wrong.

The fact that interest proceeds are created by the Texas IOLTA program does not weaken this conclusion. Rather, the simple recognition that without IOLTA there would be no interest proceeds compels it. The plaintiffs in this case are not harmed in any way by the existence of IOLTA and would not be benefitted in any tangible way by its elimination. I find it both ironic and fatal to the plaintiffs' claim that in order to have a property interest in this case,

they must rely on the existence of the program they seek to eliminate.

In addition to being consistent with a fair interpretation of the legal authority relied upon by the panel, rejection of the plaintiffs' asserted property interest in this case is consistent with the protections underlying the Takings Clause. The Takings Clause provides that "private property [shall not] be taken for public use, without just compensation." U.S. Const. amend. V. While beneficial use of property is certainly not essential to the existence of a property interest worthy of the protections of this provision, such an interest does require that the property at issue have some actual or potential *compensable value* that could accrue to the benefit of its owner. In addition, a primary purpose of the Takings Clause is to protect the investment-backed expectations of property owners that their property will not be taken for public use without just compensation.[25]

Unless the owner of a fund deposited in an IOLTA account could reasonably expect to receive interest proceeds (of any amount) from her earnings, the client's "property" does not have any compensable value. Moreover, the fact that the client does not receive any interest proceeds from her deposited funds does not interfere with her investment-backed expectations because she could not have reasonably expected to receive any net interest when the deposit was made. In my view, these unusual circumstances prevent the

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[25] In *Lucas v. South Carolina Coastal Council,* Justice Scalia noted that the Court has "acknowledged time and again, '[t]he economic impact of the regulation on the claimant and . . . the extent to which the regulation has interfered with distinct investment-backed expectations' are keenly relevant to takings analysis generally." 505 U.S. 1003, 1019 n. 8, 112 S.Ct. 2886, 2895 n. 8, 120 L.Ed.2d 798 (1992) (quoting *Pennsylvania Cent. Transp. Co. v. City of New York,* 438 U.S. 104, 124, 98 S.Ct. 2646, 2659, 57 L.Ed.2d 631 (1978)).

client from asserting a constitutionally cognizable interest in property.

This understanding of the Takings Clause is buttressed by the available remedy for plaintiffs whose property has been unconstitutionally taken. Such plaintiffs are entitled to just compensation, *i.e.*, the fair market value of their property. Because the fair market value of the earnings of IOLTA-eligible funds is $0, the client would be entitled to nothing. In sum, applying Fifth Amendment protections to an asserted property interest that does not have any compensable value is not consistent with the purposes that underlie the Takings Clause – to compensate a property owner for the value of her property that was taken for public use.

IV.

In addition to creating a circuit split, misinterpreting the legal authority upon which it relied, and applying a takings clause analysis to governmental action that does not implicate relevant fifth amendment values, the panel's analysis can only create confusion for the district court on remand. The Supreme Court's cases dealing with the Takings Clause fit roughly into the two categories of regulatory takings and per se takings. *See* JOHN E. NOWAK & RONALD D. ROTUNDA, CONSTITUTIONAL LAW § 11.12, at 462-66 (5th ed. 1995). Regulatory takings involve governmental regulations that impinge upon a property owner's economic interests. In regulatory takings cases, the Court has adopted a balancing test whereby it weighs the economic impact of the regulation on the property owner suffering the loss against the public benefits of the regulation. *See, e.g., Pennsylvania Cent. Transp. Co.*, 438 U.S. at 124, 98 S.Ct. at 2659. Viewed as a regulatory takings case, IOLTA clearly passes muster because the clients have suffered no economic loss and the public has greatly benefitted. *See Massachusetts Bar Fdn.*,

993 F.2d at 976 (noting that Massachusetts's IOLTA program has no economic impact on clients and does not interfere with their investment-backed expectations).

Per se takings involve what might be considered a "literal" taking of property. The Court adopts a per se approach and finds a compensable taking of property without a case-by-case inquiry. *See* NOWAK & ROTUNDA, *supra,* § 11.12, at 463-64. The Court has adopted a per se approach if a regulation deprives an owner of the entire value of her property. *Id.* (citing *Lucas,* 505 U.S. at 1003, 112 S.Ct. at 2886). The Court has also adopted a per se approach if the governmental action results in physical occupation of property or a permanent change in rights of ownership. *Id.* at 464 (citing *Loretto v. Teleprompter Manhattan CATV Corp.,* 458 U.S. 419, 102 S.Ct. 3164, 73 L.Ed.2d 868 (1982)). Viewed as a per se takings case whereby the clients have a property interest that is literally appropriated by the state, IOLTA is almost certainly unconstitutional.

*Webb's* was clearly a per se takings case. The Court's entire opinion is dedicated to determining that the creditors had a property right in the principal and interest proceeds of the subject interpleader fund. *See* 449 U.S. at 156-64, 101 S.Ct. at 448-53. Because this property was appropriated by the state for its own purposes, a literal taking of the property occurred. This latter conclusion required no separate analysis by the Court and accordingly was given none. *See id.* at 164-65, 101 S.Ct. at 452-53.

The panel's opinion in the instant case gave no explicit indication whether the court viewed the case as a regulatory or per se takings case. If the panel viewed this case as one involving a regulatory taking, it should have made this clear in its remand order and should not have relied on *Webb's.* On the other hand, if the panel regarded the case as one involving a per se taking, it should not have bifurcated the inquiries regarding whether the clients had a property

right and whether a taking of that property occurred. An affirmative answer to the second question would necessarily follow from an affirmative answer to the first.

The panel's opinion implicitly indicated that it left open the question of whether the case should be viewed as a regulatory takings case or as a per se takings case. The panel noted that "to prevail on their taking claim, the plaintiffs must demonstrate that the taking was against the will of the property owner." *Washington Legal Fdn.*, 94 F.3d at 1004. In addition, the court cited *Yee v. City of Escondido*, 503 U.S. 519, 539, 112 S.Ct. 1522, 1534-35, 118 L.Ed.2d 153 (1992), which held that "because [a city's] rent control ordinance [did] not compel a landowner to suffer the physical occupation of his property, it [did] not effect a per se taking. . . ." While the applicability of this decision to the context of deposited funds is not clear, it does leave open the possibility that a per se taking did not occur in the subject case because clients voluntarily deposit their money with an attorney (who, in turn, deposits eligible funds into an IOLTA account). The fact remains, however, that *Webb's*, the principal case relied upon by the panel, was a per se takings case. Because I abide by my concerns regarding the panel's conclusion that the plaintiffs asserted a constitutionally cognizable property interest in the accrued interest from IOLTA deposits, I would not burden the district court with this confusion.

V.

The issue addressed by the panel in the subject case raises very difficult and interesting conceptual issues regarding the proper definition of property for fifth amendment purposes. Three judges in this circuit have concluded that the plaintiffs have asserted a constitutionally cognizable property interest in the earnings from IOLTA-eligible funds, despite the inability of such funds to produce interest proceeds. I disagree with that conclusion, as has

every other court to have addressed the issue. Moreover, the panel's decision on this "threshold issue" will have important implications for the disposition of this case on remand and, ultimately, for the constitutionality of the IOLTA programs in Louisiana, Mississippi, and Texas. For these reasons, I believe that the intellectual efforts of our court's entire membership would have benefitted the decision making process in this clearly important case. I regret my colleagues' decision to deny rehearing en banc and respectfully dissent.

(2)

Supreme Court, U.S.
FILED
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No. 02-1

IN THE
# Supreme Court of the United States

THOMAS R. PHILLIPS, NATHAN R. HECHT, CRAIG T. ENOCH, PRISCILLA R. OWENS, JAMES A. BAKER, DEBORAH G. HANKINSON, HARRIET O'NEILL, and XAVIER RODRIGUEZ, in their official capacities as Justices of the Supreme Court of Texas; TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; and RICHARD TATE, in his official capacity as Chairman of the Texas Equal Access to Justice Foundation,
*Petitioners,*

v.

WASHINGTON LEGAL FOUNDATION, WILLIAM R. SUMMERS, and MICHAEL J. MAZZONE,
*Respondents.*

**On Petition for Writ of Certiorari to the United States Court of Appeals for the Fifth Circuit**

## MEMORANDUM OF RESPONDENTS WASHINGTON LEGAL FOUNDATION AND SUMMERS IN RESPONSE TO THE PETITION

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## QUESTIONS PRESENTED

1. Whether the Texas Interest on Lawyers' Trust Accounts ("IOLTA") program "takes" private property within the meaning of the Takings Clause of the Fifth Amendment.

2. Whether a claimant whose funds have been appropriated by government officials is entitled to relief, including injunctive or declaratory relief, under the Takings Clause.

3. Whether the Justices of the Supreme Court of Texas, in light of their role in enforcing compliance with the IOLTA program, are entitled to dismissal of the claims against them on grounds of legislative immunity from suit.

## PARTIES TO THE PROCEEDINGS

Aside from the parties named in the caption, the following were Defendants/Appellees in the court of appeals: Greg Abbott, Alberto R. Gonzales, and Wallace B. Jefferson, in their official capacities as Justices of the Supreme Court of Texas. Justice Abbott and Justice Gonzales no longer serve in those capacities and thus are no longer parties to this proceeding.

Respondent Washington Legal Foundation is a nonstock corporation; it has no parent corporation, and no publicly held company holds any of its stock.

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## MEMORANDUM OF RESPONDENTS SUMMERS AND WASHINGTON LEGAL FOUNDATION IN RESPONSE TO THE PETITION

Respondents Washington Legal Foundation (WLF) and William R. Summers respectfully file this Memorandum in partial support of the Petition for a writ of certiorari.[1] Respondents oppose the grant of the Petition as to Question Three. Respondents do not oppose the grant of the Petition as to Questions One and Two.

Questions One and Two are similar to the questions presented in *Washington Legal Found. v. Legal Found. of WA* ["*WLF v. LFW*"], No. 01-1325. The petition for a writ of certiorari in *WLF v. LFW* was granted on June 10, 2002. Accordingly, the Court may wish to grant the Petition as to Questions One and Two, or to hold the Petition in abeyance pending decision in *WLF v. LFW*. Respondents suggests that granting review as to Questions One and Two is the preferable course. The underlying factual issues have been more fully developed here than in *WLF v. LFW*; thus, granting review in this case might assist the Court in resolving the questions presented by both cases. Respondents believe that Petitioners' formulation of Question Two seriously distorts the record in this case; Respondents have restated Question Two to reflect more accurately the proceedings to date.

## STATEMENT OF THE CASE

Texas, like all other states and the District of Columbia, has established an IOLTA ("Interest On Lawyers' Trust Accounts") program. The Texas IOLTA program generates

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[1] Respondent Michael J. Mazzone is not a party to this memorandum. References herein to "Respondents" shall refer to Respondent WLF and Respondent Summers only, unless otherwise noted.

funds to be used for legal services to indigents by requiring lawyers to deposit nominal client funds and client funds held for a short duration into special IOLTA interest-bearing accounts. As with the IOLTA programs in another twenty-five states (including the State of Washington), attorney and client participation in the Texas IOLTA program is mandatory.

The individual Respondents in this case are a lawyer and a client, both of whom are impacted by the Texas IOLTA program and who object to its application to them. Michael J. Mazzone is an attorney licensed to practice law in the State of Texas. Mr. Mazzone maintains an IOLTA account into which he regularly places client trust funds that are either nominal in amount or are reasonably anticipated to be held for a short period of time.

William J. Summers is a citizen of Texas whose business dealings regularly require him to retain the services of lawyers, and those lawyers (including Mr. Mazzone) have on occasion required him to provide retainers to ensure payment of future legal bills. Those retainers have been deposited in IOLTA accounts. At all times since 1993, some of Mr. Summers's funds have been on deposit in IOLTA accounts. In light of his business dealings, he expects to continue to have such funds on deposit in IOLTA accounts for the foreseeable future. Mr. Summers repeatedly made known his objection to having his funds used to support the IOLTA program and thus objected to the placement of his retainers into IOLTA accounts. Mr. Mazzone has explained in response that, due to the relatively small size of the retainers, he was required by state law to keep the funds in IOLTA accounts.

Respondent WLF is a public interest law firm whose members include Texas lawyers similarly situated to Mr. Mazzone and Texas citizens similarly situated to Mr. Summers.

It is (and has been for centuries) a common practice for attorneys to hold funds belonging to their clients in connection with their practice of law. Indeed, the vast majority of today's attorneys could not as a practical matter operate their law practices without collecting client funds and holding them in trust for their clients. The experience of Appellant Michael Mazzone is typical of lawyers throughout the nation. He testified that, in those instances in which a client's ability to pay his/her bills was open to question, his firm felt obliged to require the client to pay a retainer that could be used to cover unpaid bills. Trial Transcript ("Tr.") 40. *See also* Def. Ex. 2 (policy of Mr. Mazzone's law firm was to obtain retainer from all new clients).

For a variety of reasons, before the advent of IOLTA programs, client trust funds often were placed in non-interest-bearing accounts. Efforts to create IOLTA programs began in the 1970s; Florida started the movement to persuade lawyers to deposit client funds in savings accounts and pay the interest to state bar organizations. Under such programs, interest earned on pooled attorney trust accounts is paid to foundations established by state supreme courts, and those foundations in turn distribute funds to groups that hire attorneys who purport to represent the interests of low-income individuals.

The IOLTA program in Texas was created by order of its Supreme Court effective May 9, 1984. The order, now codified as Article XI of the State Bar Rules, provided that an attorney receiving client funds that were "nominal in amount" or were "reasonably anticipated to be held for a short period of time" was permitted to place the funds into an unsegregated interest-bearing bank account (an "IOLTA account") and to pay interest earned on those funds to a nonprofit corporation to be established by rules to be promulgated by the Supreme

Court of Texas. TEX. STATE BAR R. art. XI, § 5, *reprinted in* TEX. GOV'T CODE ANN., tit. 2, subtit. G app. (Vernon 1984).

To implement Article XI, the Supreme Court of Texas by order dated April 30, 1984 adopted its "Rules Governing the Operation of the Texas Equal Access to Justice Program" (the "IOLTA Rules"). *See* Fifth Circuit Record Excerpts ("R.E.") 8 at 9-19. The IOLTA Rules established the Texas Equal Access to Justice Foundation ("TEAJF") as the nonprofit corporation that was to receive funds paid into the IOLTA program. Consistent with Article XI, the IOLTA Rules specified that funds forwarded to TEAJF from IOLTA accounts were to be awarded as grants solely to nonprofit organizations that "have as a primary purpose the delivery of legal services to low income persons." *Id.* at 13.

During the first four years of operation of the IOLTA program (1985-88), funds forwarded from IOLTA accounts to TEAJF never exceeded $1 million a year. On December 13, 1988, the Supreme Court of Texas amended Article XI and the IOLTA Rules to make participation in the Texas IOLTA program mandatory. Pursuant to the amended Article XI and the amended IOLTA Rules, attorneys in Texas who "hold client funds that are nominal in amount or are reasonably anticipated to be held for a short period of time" *must* place the funds in an unsegregated "interest-bearing insured depository account," with the interest earned thereon to be paid to TEAJF. Rule 4; *id.* at 9.

The issue of whether client trust funds "are nominal in amount or held for a short period of time," and thus required to be placed in IOLTA accounts, is addressed by Rule 6 of the IOLTA Rules. Rule 6 requires funds to be placed in IOLTA accounts if such funds:

> [C]ould not reasonably be expected to earn interest for the client or if the interest which might be earned on such funds is not likely to be sufficient to offset *the cost of establishing and maintaining the account*, service charges, accounting costs and tax reporting costs which would be incurred in attempting to obtain interest on such funds for the client. Also to be considered are the nature of the proceeding or transaction involved and the likelihood of delay in the need for such funds in such proceeding or transaction.

*Id.* at 11 (emphasis added).[2] In other words, attorneys are required to factor into their "net interest" calculation their firm's internal costs in establishing and maintaining an interest-bearing account for their clients, *regardless whether* (as will usually be the case) those internal costs are no greater than the internal costs associated with maintaining an IOLTA account.

The IOLTA Rules provide for severe enforcement measures against any attorney who fails to comply with IOLTA's requirements. For example, Rule 24 provides for the automatic suspension of the law license of any attorney who fails to submit an annual "compliance statement" certifying that he is maintaining an IOLTA account in accordance with the IOLTA Rules. R.E. 8, at 17.

The switch from a voluntary to a mandatory IOLTA program became effective as of July 1, 1989. As a result of that

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[2] Rule 6 was amended in 1998 in response to this lawsuit. Earlier versions of Rule 6 appeared to require that funds be placed into IOLTA accounts unless the attorney could generate *net* interest for his/her client by placing client funds in a *separate* interest-bearing account for each client's deposit. Rule 6 now states that attorneys are permitted to pool client funds in an effort to generate net interest.

switch, interest income generated by the Texas IOLTA program has increased several-fold -- to nearly $10 million dollars in its highest year. In 1998-99, TEAJF distributed $5.3 million in IOLTA-funded grants. Nationwide, IOLTA programs generate more than $120 million annually (Tr. 216), indicating that on a typical day about $10 billion in client funds is being held in IOLTA accounts.

As the district court found in its Memorandum Opinion, Mr. Summers gave Mr. Mazzone a $1,000 retainer in May 1993 to secure Mr. Mazzone's counsel in connection with litigation filed against Mr. Summers. Pet. App. 50a. Mr. Mazzone deposited those funds in his firm's IOLTA account, where they remained (and earned interest that was forwarded to TEAJF) through the time of trial in September 1999. *Id.*[3] Because Mr. Mazzone continued to represent Mr. Summers following the bankruptcy filing, Mr. Summers gave Mr. Mazzone an additional $250 retainer in August 1999, and those funds were also deposited in the IOLTA account of Mr. Mazzone's law firm. *Id.* The district court found that Mr. Mazzone's decision to deposit the two retainers in his firm's IOLTA account was in accord with the IOLTA Rules. *Id.* 51a.

Respondents filed suit against the Texas IOLTA program in February 1994 in U.S. District Court for the Western District of Texas. Named as defendants were TEAJF; the Chairman of TEAJF, in his official capacity only; and the nine

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[3] As a result of litigation-related indebtedness, Mr. Summers filed a Chapter 7 bankruptcy petition in June 1999. *Id.* 51a. Mr. Mazzone's law firm was one of Ms. Summers's creditors. After trial and with the permission of the bankruptcy court, the law firm took Mr. Summers's $1,000 retainer as partial payment of his unpaid legal bills.

Justices on the Supreme Court of Texas, in their official capacities only (the "Justices").[4]

In January 1995, the district court granted TEAJF's motion for summary judgment. Pet. App. 147a-168a. The court found that IOLTA depositors lacked any property rights in the interest generated by their funds; and that in the absence of such rights, they could not state claims under either the Fifth Amendment's Takings Clause or the First Amendment.

In September 1996, in an opinion written by Judge John Minor Wisdom, the U.S. Court of Appeals for the Fifth Circuit reversed the grant of summary judgment for TEAJF and remanded the case to the district court for further proceedings. Pet. App. 127a-146a. Labeling the IOLTA program a "modern-day attempt at alchemy" whose supporters claim to have created property from nothing, the court concluded that "it seems obvious that the interest earned in the IOLTA accounts is the property of the clients whose money is held in those accounts." *Id.* 133a-134a. The court declined to determine whether IOLTA violated Respondents' constitutional rights; rather, it remanded the case "for reconsideration in light of the principles explained in this decision and for further factual development of the record." *Id.* 144a. The court affirmed the district court's dismissal of Respondents' claim for a refund of money paid to TEAJF, holding that TEAJF is an arm of the State of Texas and thus possesses Eleventh Amendment immunity from damage claims. *Id.* 145a-146a.

This Court later agreed to review the Fifth Circuit's decision, limited to the issue of whether "interest earned on client trust funds held by lawyers in IOLTA accounts [is] a

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[4] Except as otherwise indicated, the term "TEAJF" will refer to Petitioners collectively.

property interest of the client or lawyer, cognizable under the Fifth Amendment of the United States Constitution, despite the fundamental precept of IOLTA that such funds, absent the IOLTA program, could not earn interest for the client or lawyer." 521 U.S. 1117 (1997). In June 1998, the Court answered that question affirmatively and affirmed the Fifth Circuit, holding that interest paid on IOLTA accounts belongs to those whose funds generated the interest. Pet. App. 100a-126a. The Court explained that IOLTA depositors have property rights in the interest income, even though "the interest income at issue here may have no economically realizable value to its owner." *Id.* 112a.

On remand, the district court conducted a non-jury trial in September 1999. On January 4, 2000, the district court granted the Justices' motion for judgment on the pleadings, on the ground that the Justices were legislatively immune from suit. *Id.* 86a-99a. On January 28, 2000, the district court issued a Memorandum Opinion and Order dismissing all remaining claims; the judge found that TEAJF's confiscation of Respondents' property violated neither the Fifth nor First Amendments. *Id.* 44a-85a.

The Fifth Circuit on October 15, 2001 reversed and remanded, with Judge Wiener dissenting. *Id.* 1a-43a. The court ruled that TEAJF's appropriation of property belonging to Respondents -- in the absence of evidence that TEAJF's actions amounted to a tax, user fee, or similar exaction -- was subject to "per se [Takings Clause] analysis" and thus violated the Takings Clause. *Id.* 9a-16a. Turning to the issue of relief, the Court noted that, because TEAJF had succeeded in eliminating Respondents' damage claims by raising an Eleventh Amendment defense, the precise amount of Respondents' loss was not relevant; it was enough, to establish a claim for declaratory and injunctive relief, that Respondents had

demonstrated that they were deprived of property having *some* value. *Id.* 14a-17a. The appeals court rejected TEAJF's contention that damages are the only appropriate remedy for a Takings Clause violation, finding both that TEAJF had conceded (in the prior appeal) that it was subject to prospective injunctive relief for Takings Clause violations and that injunctive relief was proper under the facts of this case. *Id.* 17a-25a. The court also rejected TEAJF's claim (raised for the first time five years after suit was filed) that the Takings Claim was not ripe for review because Appellees did not seek relief in a state forum before filing suit. *Id.*

Finally, the appeals court rejected the Justices' claim that they were legislatively immune from suit. *Id.* 26a-27a. The court found that the Justices played a role in enforcing the IOLTA program, and that they could not invoke legislative immunity to bar judicial review of those enforcement activities. *Id.*

The court remanded the case to the district court for entry of appropriate declaratory and injunctive relief. *Id.* 27a. In light of its ruling, the appeals court found it unnecessary to address Respondents' claims that: (1) the district court failed to address Respondents' trial evidence that virtually all IOLTA depositors would be better off if permitted to opt out of the IOLTA program; and (2) the IOLTA program violated their First Amendment rights.

In June 2002, the Fifth Circuit denied Petitioners' motion for rehearing *en banc*. *Id.* 169a-170a. Seven of the 15 active judges on the appeals court dissented from that denial. *Id.* 170a-171a.

## REASONS FOR GRANTING THE WRIT ON QUESTIONS ONE AND TWO

Respondents support granting the writ on Question One and Two, but submit that the Fifth Circuit's decision ultimately should be affirmed.

*Phillips v. Washington Legal Found.*, 524 U.S. 156 (1998), established that IOLTA interest is the property of those clients whose funds generated the interest. TEAJF insists nonetheless that its confiscation of that property does not constitute a "taking" within the meaning of the Fifth Amendment, and alternatively that the "just compensation" it owes is zero even though the property it confiscated has a readily ascertainable value. This Court has *never* denied Fifth Amendment relief in a case raising even remotely similar facts.

In this case, the Fifth Circuit correctly concluded that TEAJF's confiscation of Respondents' property amounted to a Fifth Amendment taking and that Respondents were entitled to a remedy. The Fifth Circuit also correctly concluded that, in light of the unavailability of a damages remedy under the facts of this case, Respondents were entitled to entry of declaratory and injunctive relief. However, as TEAJF notes in its Petition, the Fifth Circuit's decision on each of those points conflicts directly with the Ninth Circuit's *en banc* decision in *WLF v. LFW*. In light of that conflict and the Court's June 10, 2002 decision to grant review in *WLF v. LFW*, it would be appropriate for the Court either to grant this Petition as to Questions One and Two, or to hold the Petition in abeyance pending a decision in *WLF v. LFW*.

Respondents agree with TEAJF that the more appropriate course may be to grant the Petition as to Questions One and Two and consolidate the case with *WLF v. LFW*. Unlike *WLF*

*v. LFW*, this case has been tried, and findings of fact have been made. The more complete factual record in this case may assist the Court in resolving the legal issues common to the two cases. That is particularly true with respect to the availability of declaratory and injunctive relief. The Ninth Circuit provided only a very abbreviated discussion of its decision that such relief is unavailable to IOLTA depositors; in contrast, the Fifth Circuit explained its contrary decision at length and in the context of a full record. Pet. App. 17a-25a. Respondents also agree with TEAJF that the Texas IOLTA program is somewhat more representative of IOLTA programs nationwide than is the Washington State IOLTA program at issue in *WLF v. LFW*. While the challenges to the two programs raise virtually identical legal issues, *WLF v. LFW* does so in the context of the application of IOLTA to the real estate escrow industry, and most IOLTA programs apply only to lawyers.

## I. GRANTING REVIEW ON QUESTION ONE WILL ASSIST THE COURT IN DECIDING WHETHER THE CONFISCATION OF IOLTA INTEREST VIOLATES THE TAKINGS CLAUSE

Respondents agree with TEAJF that the Fifth Circuit's decision is in direct conflict with the Ninth Circuit's decision in *WLF v. LFW* that the confiscation of IOLTA interest does not violate the Takings Clause. The Fifth Circuit held that Respondents' Takings Clause claims were subject to "per se analysis" as set forth in *Loretto v. Teleprompter Manhattan CATV Corp.*, 458 U.S. 419 (1982), and similar cases. Pet. App. 9a-12a. Applying that analysis, the court concluded that the confiscation of Respondents' interest income violated their rights under the Takings Clause, without regard to whether they could have earned "net interest" on their own in the absence of an IOLTA program. *Id.* 9a-16a & n.10. In contrast, the Ninth Circuit held that Takings Clause claims

raised by IOLTA depositors were *not* subject to per se analysis but rather should be analyzed under the *ad hoc* inquiry set forth in *Penn Central Transportation Co. v. City of New York,* 438 U.S. 104, 124 (1978). *WLF v. LFW,* 271 F.3d 835, 857 (9th Cir. 2001). Applying that *ad hoc* approach, the Ninth Circuit determined that the confiscation of the IOLTA depositors' property did not violate the Takings Clause. *Id.* at 861.

By agreeing to review *WLF v. LFW,* the Court has agreed to decide both the appropriate analysis to apply to the Takings Clause claims of IOLTA depositors and, if an *ad hoc* approach is deemed appropriate, whether the Ninth Circuit applied it properly to IOLTA depositors. The Court's analysis of those issues would be assisted if it had Respondents' claims before it at the same time. As noted above, no trial has taken place in *LFW v. WLF*; the case is before the Court on the district court's grant of summary judgment to the Washington defendants. Because a trial has taken place in this case, the Court's examination of these basic Takings Clause issues may be facilitated by inclusion of the trial record below. For example, the uncontested evidence at trial was that $1,000 belonging to Mr. Summers sat in an IOLTA account from 1993 to 1999 despite Mr. Summers's objections, that interest was earned on those funds at rates varying from .9% to 2% per year, and that the interest was forwarded on a regular basis from the IOLTA account maintained by Mr. Mazzone's law firm to TEAJF. There is no similar trial evidence in *LFW v. WLF*; the only evidence that the plaintiffs' funds were being confiscated by Washington State IOLTA authorities takes the form of affidavits and declarations in support of the plaintiffs' motion for summary judgment.

Review of Question One is also appropriate because the Texas case arises in a context more typical of IOLTA

programs nationwide than is the Washington State IOLTA program. The Washington program is unique in that it applies not only to tr ıst funds being held by attorneys but also to escrow funds being held by escrow companies and title companies in connection with real estate transactions. Moreover, the plaintiffs in *WLF v. LFW* all challenge IOLTA in the context of its application to real estate transactions. Respondents do not believe that this factual distinction between the cases will affect the Takings Clause analysis in any way. Nonetheless, if the Court limits it review of IOLTA programs to one involving real estate transactions, the applicability of the Court's ultimate decision in the case to lawyers-only IOLTA programs may be subject to question. By granting review on Question One, the Court can ensure that its decision will settle whether lawyers-only IOLTA programs can withstand Takings Clause challenge. That issue has been nanging over IOLTA programs ever since the Court's 1998 decision in *Phillips*; resolving that issue once and for all in the coming year would serve the interests of both the legal profession and the general public.

## II. GRANTING REVIEW ON QUESTION TWO WILL ASSIST THE COURT IN DECIDING WHETHER IOLTA DEPOSITORS ARE ENTITLED TO A REMEDY FOR ANY TAKINGS CLAUSE VIOLATION

Respondents agree with TEAJF that the Fifth Circuit's decision is in conflict with the Ninth Circuit's decision in *WLF v. LFW* that IOLTA depositors are not entitled to a remedy for any Takings Clause violation. The Fifth Circuit held that Respondents were entitled to a remedy for their loss of property rights, regardless whether those rights had economically realizable value. Because Texas had not provided Respondents with any means of obtaining monetary

compensation, the court held that Respondents were entitled to declaratory and injunctive relief. Pet. App. 16a-25a. In contrast the Ninth Circuit held that even if the Washington IOLTA program violated the Takings Clause, IOLTA depositors were not entitled to any compensation because the compensation due under the Fifth Amendment is zero where the depositors could not have earned net interest on their funds if allowed to opt out of the IOLTA program. *WLF v. LFW*, 271 F.3d at 864. The Ninth Circuit also held that those claiming to have been injured by the Washington IOLTA program could not sue for declaratory or injunctive relief under the Takings Clause because monetary compensation is the only permissible remedy in such cases. *Id.* at 848-50.

The Questions Presented in *WLF v. LFW* ask the Court to consider what compensation, if any, is due IOLTA depositors whose interest income has been confiscated by the State of Washington, and whether declaratory or injunctive relief is available to prevent any such confiscation that violates the Takings Clause. The Court's analysis of those issues would be assisted if it had Respondents' claims before it at the same time. In both cases, there has been considerable disagreement among the parties regarding how the loss, if any, suffered by IOLTA depositors should be measured. Those disagreements have led to confusion by the reviewing courts regarding loss claims.

IOLTA supporters (both here and in *WLF v. LFW*) have sought to measure loss by reference to the income-generating potential of IOLTA deposits if IOLTA depositors were permitted to opt out of the IOLTA program. The district judge in this case agreed with that basis of measurement; after making a factual finding that Mr. Summers and similarly situated IOLTA depositors could not generate net income on their trust funds if left to their own devices, the district judge

ruled that Respondents had not suffered any loss compensable under the Takings Clause. Pet. App. 74a. The Ninth Circuit ruled to the same effect. *WLF v. LFW,* 271 F.3d at 864. Respondents, on the other hand, have argued that loss should be measured based on the world as it is; because property with a readily ascertainable value has been confiscated from IOLTA depositors, they have suffered a loss. The Fifth Circuit agreed with that approach. Pet. App. 14a-17a. Respondents have argued alternatively that loss should be measured by whether IOLTA deposits would create actual income to the clients if they were allowed to opt out of the IOLTA program, even if that income might be eaten up by bank fees and their attorneys' overhead charges. *See, e.g., Phillips,* Pet. App. 112a ("The government may not seize rents received by the owner of a building simply because it can prove that the costs incurred in collecting the rents exceed the amount collected."). The full trial record available in this case may facilitate the Court's determination of whether IOLTA depositors suffer any loss for which the Takings Clause requires a remedy.

This case's full trial record may be particularly helpful in determining whether declaratory and injunctive relief are permissible remedies in Takings Clause challenges to IOLTA programs. The Ninth Circuit in *WLF v. LFW* said that such relief is not available, but it did so on the basis of a thin record and with little discussion. *WLF v. LFW*, 271 F.3d at 848-50. In contrast, the trial record in this case contains significant evidence that provides context to the equitable relief issue; and the Fifth Circuit considered the issue at length before determining that such relief is available to Respondents. Pet. App. 16a-25a.

## REASONS FOR DENYING THE WRIT ON QUESTION THREE

Although Questions One and Two presented by Petitioners are worthy of this Court's certiorari jurisdiction, Question Three -- whether the Justices are entitled to legislative immunity -- is not.

### I. THE APPEALS COURT CORRECTLY DECIDED THE ISSUE OF LEGISLATIVE IMMUNITY, AND PETITIONERS HAVE NOT POINTED TO ANY CIRCUIT CONFLICTS OR CONTROLLING AUTHORITY THAT WAS NOT HEEDED

The Fifth Circuit's determination that the Justices are not entitled to legislative immunity from Respondents' Fifth Amendment claims is not worthy of further review by this Court. Petitioners have cited no court of appeals decision that conflicts with the Fifth Circuit's determination. The sole Court decision upon which Petitioners rely, *Supreme Court of Virginia v. Consumers Union of the United States, Inc.* ["*Consumers Union*"], 446 U.S. 719 (1980), is also the decision upon which the Fifth Circuit principally relied in rejecting immunity. Petitioners do not disagree with the Fifth Circuit's interpretation of *Consumers Union*, but rather with its determination that the actions of which Respondents complain are not legislative in nature. That disagreement is not sufficiently weighty to justify review by this Court.

There is no question that lawmakers (including judges when acting legislatively) are immune from suit for their legislative acts. *Consumers Union,* 446 U.S. at 731-34. Thus, the Justices of the Texas Supreme Court are entitled to legislative immunity from any claim that they acted unconstitutionally in adopting the IOLTA program. But

Respondents named the Justices as defendants not because they *adopted* the IOLTA Rules but because they *enforce* them.

In 1999, five years after suit was filed, the Justices argued for the first time that they are entitled to legislative immunity -- on the ground that the power to enforce the IOLTA rules lies elsewhere. The Justices have waived the argument because their delay has prejudiced Respondents; had it been raised earlier, Respondents would have had ample opportunity to substitute in as a defendant the individual(s) determined to possess enforcement authority.

In any event, the Fifth Circuit's decision that the Justices possess IOLTA enforcement authority (and thus are not entitled to legislative immunity) is correct. IOLTA Rule 24 provides for the automatic suspension *by Texas Supreme Court personnel* of any attorney who persists in not filing an annual statement indicating that he is compliance with the IOLTA Rules. Moreover, Rule 25 permits attorneys to seek an exemption from any of the IOLTA Rules (including Rule 24), and the Justices are the final arbiters of any exemption request.

In the Fifth Circuit, the Justices argued that they were entitled to immunity because they act in their *judicial* capacity, not their enforcement capacity, when they exercise their Rule 24 and Rule 25 powers. However, this Court has held that judges are *not* entitled to judicial immunity from suits seeking declaratory or injunctive relief with respect to their judicial acts. *Pulliam v. Allen*, 466 U.S. 522, 541-42 (1984) ("judicial immunity is not a bar to prospective injunctive relief against a judicial officer acting in her judicial capacity").

When this case returns to the district court, the Justices will have an opportunity to raise issues regarding the proper scope of any equitable relief, to ensure that the relief does not

impinge upon their legislative powers. The Fifth Circuit's determination that the Justices immunity is limited to matters involving the exercise of their legislative powers is unremarkable and does not warrant further review.

## CONCLUSION

For the foregoing reasons, the Petition should be granted as to Questions One and Two and denied as to Question Three.

Respectfully submitted,

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No. 02-1

IN THE

# Supreme Court of the United States

THOMAS R. PHILLIPS, Chief Justice, NATHAN R. HECHT, Justice, CRAIG T. ENOCH, Justice, PRISCILLA R. OWENS, Justice, JAMES A. BAKER, Justice, Justice, DEBORAH G. HANKINSON, Justice, HARRIET O'NEILL, Justice, and XAVIER RODRIGUEZ, Justice, in their official capacities as Justices of the Supreme Court of Texas, TEXAS EQUAL ACCESS TO JUSTICE FOUNDATION; and RICHARD TATE, in his official capacity as Chairman of the Texas Equal Access to Justice Foundation,

*Petitioners,*

v.

WASHINGTON LEGAL FOUNDATION, WILLIAM R. SUMMERS, AND MICHAEL J. MAZZONE,

*Respondents.*

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE FIFTH CIRCUIT

## PETITIONERS' REPLY BRIEF

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## PETITIONERS' REPLY BRIEF

1. a. Respondents agree with Petitioners that the Petition should be granted as to Questions One and Two. *See* Br. in Opp. 1, 10-15, 18. Respondents agree (Br. in Opp. 1) that "the preferable course" is "granting review as to Questions One and Two" rather than holding the Petition in abeyance pending a decision in *Washington Legal Foundation v. Legal Foundation of Washington* ("*WLF v. LFW*"), No. 01-1325 (cert. granted June 10, 2002).

Respondents concur with Petitioners that "[t]he underlying factual issues have been more fully developed here than in *WLF v. LFW*," and therefore "granting review in this case might assist the Court in resolving the questions presented by both cases." Br. in Opp. 1; *see also id.* at 12 ("Because a trial has taken place in this case," but not in *WLF v. LFW*, "the Court's examination of these basic Takings Clause issues may be facilitated by inclusion of the trial record below."). In particular, Respondents note that "[t]he full trial record available in this case may facilitate the Court's determination of whether IOLTA depositors suffer any loss for which the Takings Clause requires a remedy." *Id.* at 15. Similarly, a full trial record "may be particularly helpful in determining whether declaratory and injunctive relief are permissible remedies in Takings Clause challenges to IOLTA programs." *Id.*

Respondents also agree with Petitioners that granting review in this case is "appropriate because the Texas case arises in a context more typical of IOLTA programs nationwide than is the Washington State IOLTA program." *Id.* at 12-13. "The Washington program is unique in that it applies not only to trust funds being held by attorneys but also to escrow funds being held by escrow companies and title companies in connection with real estate transactions." Br. in Opp. 13. In addition, "the plaintiffs in *WLF v. LFW* all

challenge IOLTA in the context of its application to real estate transactions." *Id.*[1]

b. If the Court chooses to grant the Petition in this case, Petitioners are prepared to make adjustments to the usual schedule for briefing and oral argument to permit this case to be argued and decided together with *WLF v. LFW*. *See* Pet. 24. In particular, Petitioners are prepared to file their opening brief in fewer than the 45 days usually allowed under the Court's rules.[2] The Court may find it worthwhile to set both cases for oral argument on the same day and allow a total of two hours for oral argument.

2. Respondents part company with Petitioners as to Question 3, concerning the immunity of the Justices of the Texas Supreme Court. Respondents urge the Court to deny the Petition as to Question 3, on the grounds that the issue has been waived and involves only an "unremarkable" application of law to a particular set of facts. Br. in Opp. 16-18. Respondents are mistaken on both counts.

*First*, the Justices have not waived their claim to legislative immunity, nor have they prejudiced Respondents.

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[1] Respondents in *WLF v. LFW* are also on record that consideration of the Texas case, with its full trial record, may assist the Court in resolving the constitutional issues presented in both cases. No. 01-1325 LFW Br. in Opp. 17-18 ("*TEAJF* itself would provide the Court with a vehicle to decide [the constitutional] issues within the same action as *Phillips*, and with the benefit of a full trial on the merits following the Court's remand in *Phillips*. The existence of factual findings from a trial record, as opposed to the summary judgment record in this case, might prove useful to the Court in resolving the issues.")

[2] If the Court is inclined to grant the Petition and hear this case together with *WLF v. LFW*, it may wish to consider the Petition on August 25 or September 6. This would have the effect of accelerating the briefing on the merits.

The Justices asserted legislative immunity in a motion for judgment on the pleadings filed more than seven months before trial. Respondents never moved to strike the Justices' motion, never sought to compel the Justices to disclose the proper defendants, and never asserted any prejudice in the trial court, where the matter could have been easily remedied. The Respondents could not have been prejudiced in any case, because the identity of persons having independent enforcement power is clearly described in the Rules Governing the Operation of the Texas Equal Access to Justice Program (specifically, in Rule 240).

*Second*, the Texas Justices do not contend that the scope of their official immunity is, in and of itself, sufficiently important to justify further review. Rather, they urge that if this Court grants certiorari as to Questions One and Two, the immunity issue warrants review as an additional question presented.

Respondents assert (Br. in Opp. 16) that the Justices "do not disagree with the Fifth Circuit's interpretation of" *Supreme Court of Virginia v. Consumers Union of the United States, Inc.*, 446 U.S. 719 (1980). That is not so. The Fifth Circuit's expansive reading of "enforcement" acts, which subjects state high courts to claims for prospective relief, virtually nullifies the legislative immunity that *Supreme Court of Virginia* extended to justices acting in their legislative capacity. *Id.* at 734. In that case, the Court held that the Virginia Court was cloaked with absolute immunity for its legislative acts, but was not shielded from claims for declaratory and injunctive relief arising out of enforcement acts.

This conclusion – that the Virginia Court and its chief justice were properly held liable in their enforcement capacities – hinged on various sections of the Virginia Code of Professional Responsibility authorizing the high court to

exercise "independent authority of its own to initiate proceedings against attorneys." *Id.* at 736. That is, the Virginia Court was found to have power beyond that of merely adjudicating complaints filed by others and beyond the courts' normal authority to sanction attorneys for contempt.

This critical distinction – independent authority to initiate proceedings for non-compliance – was omitted altogether from the Fifth Circuit's analysis. Indeed, the appellate court found the procedure established by Rule 24 sufficient to subject the Justices to claims for prospective relief, even though the rule itself makes clear that independent enforcement authority does not lie with the Justices.

Rule 24 requires a Texas attorney to provide annually a written statement of IOLTA compliance *to the TEAJF*. If the attorney fails to do so, *TEAJF* contacts the attorney and attempts to resolve the non-compliance administratively. If the attorney still refuses to comply, the *State Bar of Texas* notifies the Texas Supreme Court *Clerk* – not the Justices – and the clerk automatically places the attorney on a suspension list until the compliance statement is filed. *See* TEAJF Rule 24; *Washington Legal Found. v. TEAJF*, 86 F. Supp.2d 617, 622 (W.D. Tex. 2000).

Respondents also point to Rule 25 as further evidence of the Justices' enforcement powers. But the Justices do not have independent authority to initiate proceedings under Rule 25 either. That rule provides for judicial review of adverse decisions of the Board of Directors for the State Bar, when an attorney requests an exemption from the IOLTA program, an extension of time to comply with a deficiency notice, or an extension of time to file a compliance statement. Moreover, Rule 25 has no relationship to this case, or to Rule 24. The

two rules cannot be reasonably read in conjunction, so as to find enforcement authority on the part of the Justices.

## CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted,

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